92-2041

No. _____

Supreme
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In The

Supreme Court of the United States

October Term, 1992

Swarovski International Trading Corporation, A.G., Swarovski Management and Consulting, A.G., D. Swarovski & Co., Swarovski Aktiengesellschaft, and Swarovski America Limited,

Petitioners,

versus

Ebeling & Reuss, Ltd. t/a Ebeling & Reuss Company,

Respondent.

Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. Whether a federal court may enter judgment for punitive damages in the amount of a jury's answer to a single punitive damage interrogatory after that court has found, as a matter of law, that no liability exists on one or more of the causes of action for which the jury was instructed that it could award punitive damages, a question as to which the courts of appeals are in conflict.

2. Whether Swarovski's procedural due process rights, including its right to appropriate and meaningful appellate review recognized in *Pacific Mutual Life Insurance Co. v. Haslip*, 111 S. Ct. 1032, 1045 (1991), were violated by the Third Circuit's affirmance of the punitive damage award without any written opinion or explanation of reasons in support of the judgment.

3. Whether the excessive and disproportionate nature of the $16,500,000 punitive damage award, based on the claim that Swarovski fraudulently induced Ebeling & Reuss, Ltd. into an exclusive distribution contract, violated Swarovski's substantive due process rights.

PARTIES TO THE PROCEEDINGS

The parties to the proceedings below were the Petitioners Swarovski International Trading Corporation, A.G.; Swarovski Management & Consulting, A.G.; D. Swarovski & Co.; Swarovski Aktiengesellschaft; and Swarovski America Limited and Respondent Ebeling & Reuss Ltd. t/a Ebeling & Reuss Company.

Petitioners have no parent companies or subsidiaries to list pursuant to this Court's Rule 29.1.

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Petitioners Swarovski International Trading Corporation, A.G.; Swarovski Management & Consulting, A.G.; D. Swarovski & Co.; Swarovski Aktiengesellschaft and Swarovski America Limited (hereinafter jointly referred to as "Swarovski") respectfully pray that a writ of certiorari issue to review the judgment entered below by the United States Court of Appeals for the Third Circuit on April 7, 1993.

OPINIONS BELOW

This is a petition for a writ of certiorari to the United States Court of Appeals for the Third Circuit (the "Third Circuit") to review an unreported decision of that Court. The Court issued its decision in the form of a Judgment Order, which is reprinted in the Appendix at 1-2. The ruling of the Third Circuit on the Petition for Rehearing and Rehearing In Banc is not reported, and is reprinted in the Appendix at 3-4. The opinion of the district court is not reported, and is reprinted in the Appendix at 5-77.

JURISDICTION

The case below was filed in the Eastern District of Pennsylvania on the assertion by Plaintiff Ebeling & Reuss, Ltd. of diversity of citizenship under 28 U.S.C. § 1332(a) (Supp. 1991). The judgment of the United States Court of Appeals for the Third Circuit was entered on April 7, 1993. Petitioners' timely filed Petition for Rehearing and Rehearing In Banc was denied on May 17, 1993. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISIONS INVOLVED

The Seventh Amendment to the United States Constitution provides, in relevant part:

> In Suits at common law . . . , the right of trial by jury shall be preserved, and no fact tried by a jury shall be otherwise re-examined in any

> Court of the United States, than according to the rules of the common law.

U.S. Const. amend. VII.

The Fourteenth Amendment to the United States Constitution provides, in relevant part:

> No State shall . . . deprive any person of life, liberty, or property, without due process of law. . . .

U.S. Const. amend. XIV.

STATEMENT OF THE CASE

The instant case arose out of an alleged exclusive distribution contract between Ebeling & Reuss, Limited ("E&R"), an American company engaged in the business of distributing and marketing giftware in the United States, and the largely Austrian based Swarovski Defendants, who are engaged in the manufacture of fine crystal. *See* Rec. 2645a.[1] At trial, E&R contended that a series of oral and written communications in late 1985 and early 1986 culminated in an agreement granting E&R the exclusive right to distribute all miniature crystal figurines manufactured by Swarovski's injection molding technology. *See* Rec. 1776a, 4346a. Although the parties eventually exchanged drafts of a comprehensive written agreement, *see* Rec. 1979a; 4105-71a; 4140-52a; 4555-64a, it is undisputed that no version of the draft contracts was ever executed.

[1] The record in the United States Court of Appeals for the Third Circuit is cited herein as "Rec.".

From late 1986 through the time E&R initiated suit in June 1988, Swarovski filled E&R's purchase orders for the crystal figurines, which E&R marketed under the name "Crystal Signatures." E&R sold $60,655 of Crystal Signatures to retailers in January 1987; $106,697 in February; $135,658 in March; $85,864 in April; and $28,680 in May. *See* Rec. 3200-01a. Sales remained at the spring of 1987 level for the duration of the Crystal Signatures program. One year after the initial purchase order, E&R placed a second order, for only one-half the quantity of figurines in the first. *See* Rec. 4123-24a. A third purchase order followed several months thereafter, for one-half the quantity of figurines in the second. *See* Rec. 4199-4200a. Each order was for different figurines. No re-orders were ever placed. *See* Rec. 2490-91a.

On March 31, 1988, E&R Company, the entity with which Swarovski had been dealing in connection with the Crystal Signatures line and an unincorporated division of Alco Standard Corporation, a multi-billion dollar conglomerate, was sold in a leveraged buyout for $4.7 million, including a $1.2 million promissory note, *see* Rec. 4325-39a, to a group of investors and current officers. Following the leveraged buyout, the parties were unable to reach agreement on the proposed written contract. Based on the parties' failure to reach a comprehensive written agreement, the poor performance of the Crystal Signatures line, and the change in E&R's ownership and financial condition, Swarovski notified E&R on June 1, 1988 that it did not have Swarovski's consent to the shipment of product or the use of Swarovski's name, unless and until an agreement could be reached. *See* Rec. 4396a. On June 20, 1988, E&R filed suit.

At trial, E&R's case consisted primarily of the testimony of Michael Russo ("Russo"), one of its owner/officers, and Stephen Cook ("Cook"), E&R's expert witness on damages. Russo testified that the discussions and communications during the first half of 1986 culminated in an agreement on July 22, 1986, *see* Rec. 1855-56a; 3316a, pursuant to which E&R held the exclusive right to *all* injection molded figurines manufactured by Swarovski, *see* Rec. 2144a, for the life of the product cycle, *see id.*, a period which he defined to mean for as long as E&R "chose to continue producing it and selling it." Rec. 1856a. This agreement, Russo asserted, had been assigned to E&R, Ltd. in the buyout. In addition, Russo testified that the poor sales of the Crystal Signatures line were due to a February 2, 1987 letter of Swarovski America Ltd. (Swarovski's United States distribution subsidiary) to its retailers criticizing the E&R line and to late deliveries of merchandise by Swarovski in 1986. *See* Rec. 1918-19a; 1931-32a and 1948-49a.

With respect to damages, Cook testified that various unspecified retail stores would have spent $322 million to purchase injection molded figurines from E&R over a twelve year period. *See* Rec. 4527a. In calculating this figure, Cook relied on E&R's 1986 sales projection, which had been drafted for use in a sales presentation to Swarovski. *See infra* App. 38. Cook testified that all these sales would have resulted in a profit of $49 million to E&R in present value terms. *See* Rec. 2293-94a.

The district court sent the case to the jury in three stages. In the first stage, the jury was asked to render liability findings on E&R's common law claims, including a claim for breach of contract and multiple claims of

fraud. In the second stage, the jury was asked to make damage findings, both actual and punitive, in connection with E&R's common law claims. In the third and final stage, the jury was asked to make liability and damage findings on E&R's claims relating to unfair competition, including trademark infringement and misuse of trade secrets. The jury returned findings in favor of E&R on all claims, awarding in excess of $55,000,000 against Swarovski. *See infra* App. 5.

On August 25, 1992, the district court ruled on the post-trial motions of both parties. *See infra* App. 5-77. In its Memorandum and Order (the "Opinion"), the district court upheld the jury's findings on E&R's breach of contract and on one of its fraud claims, and entered judgment on those claims in the amount of $42,350,000, consisting of $850,000 in out-of-pocket expenses, $25,000,000 in lost profits, and $16,500,000 in punitive damages. The punitive damage figure had been returned by the jury in response to a single interrogatory premised on five separate tort claims. *See infra* App. 89.

The breach of contract claim and the sole upheld claim of fraud were closely related. On the breach of contact, the district court found that E&R "had the exclusive contractual right to market the entire product line for the life of the products." *See infra* App. 13-14. Similarly, in connection with E&R's claim of fraud, the district court found sufficient evidence that Swarovski had "misrepresented to E&R that they intended to give E&R the exclusive distribution rights to the injection molded crystal figurines line." App. 23. Although E&R argued that it had five separate and distinct claims of fraud against Swarovski, *see* Rec. 3253-56a; 3337-41a, the district court

grouped these five claims into two different categories, characterizing the first as fraud against E&R Company (Plaintiff's predecessor in interest) and the second as fraud against E&R Ltd. (the entity created in the leveraged buyout). *See infra* App. 22-26. The district court then granted the Defendants judgment notwithstanding the verdict on the second class of fraud claims.

In connection with the award of $16,500,000 in punitive damages, the district court upheld this award based on the following explanation:

> The punitive damages are not disproportionate to the nature of defendants' actions. Defendants were using their capacity to make injection molded figurines to compete with E&R, Ltd. while refusing to deliver the Disney figurines in breach of contract. *The jury also saw and obviously reacted to the arrogance of defendants' witnesses. The jury clearly found defendants' conduct outrageous as it found against defendants on all counts.*
>
> The punitive damages are not disproportionate to the nature and extent of the harm. The resulting total award of $16,500,000 in punitive damages is less than the total award of $25,850,000 in compensatory damages. Plaintiff's business was in effect destroyed by defendants' conduct; plaintiff ultimately filed for bankruptcy protection. *The award of punitive damages is not excessive even though the court will set aside the jury findings on liability for tortious interference and fraud against E&R, Ltd.* The jury determined the amount of punitive damages based on the nature of defendants' actions, not the theory of defendants' liability.

> The defendants' net worth was stipulated to be in excess of $200 million dollars. The punitive damage award of $16.5 million is less than 10% of that amount. Considering the conduct of defendants, the harm to plaintiff that defendants intended to cause to avoid the contract, and *the extreme wealth of defendants (far in excess of the amount stipulated)*, this court is not persuaded to reduce the punitive damage award further.[2]

See infra App. 46 (emphasis added).

On April 7, 1993, the United States Court of Appeals for the Third Circuit affirmed the judgment of the district court without a written opinion or explanation of reasons supporting its decision, and without adopting the Opinion of the district court. Thereafter, on May 17, 1993, the Third Circuit denied Swarovski's Petition for Rehearing and Rehearing In Banc. *See infra* App. 3-4. Again, the Third Circuit gave no explanation of reasons supporting its decision or the award of $16,500,000 in punitive damages.

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[2] The punitive damage award on the fraud claims was not reduced by the district court at all. Rather, the district court granted the Swarovski Defendants judgment notwithstanding the verdict on all of E&R's trademark and unfair competition claims. As a result, a total of $5 million in punitive damages, awarded by the jury in answer to separate interrogatories, was not included in the final judgment. *See infra* App. 45.

REASONS FOR GRANTING THE WRIT

The Third Circuit's disposition of Swarovski's appeal has created a conflict with the law of other Circuits concerning the right of a federal court to apportion punitive damages among particular causes of action when the jury did not apportion them and when certain of the tort claims upon which the award was based did not survive review. Furthermore, by employing the device of the judgment order, a summary affirmance without opinion, to confirm a judgment which includes an award of $16.5 million in punitive damages, the Third Circuit failed in its constitutionally mandated task under this Court's decision in *Pacific Mutual Life Ins. Co. v. Haslip*, 111 S. Ct. 1032 (1991), to review the punitive damage award, and thereby violated Swarovski's procedural due process rights. This failure to conduct and articulate its required review of the punitive damages has hidden significant legal deficiencies in the award. Based on these deficiencies, the punitive damage award is unconstitutionally excessive, disproportionate to the nature of Swarovski's conduct, and in violation of Swarovski's substantive due process rights.

A. The District Court Improperly Allocated the Entire Punitive Damage Award To the One Affirmed Claim of Fraud.

In answer to a single interrogatory, the jury awarded $16.5 million in punitive damages based on its liability findings on E&R's multiple claims of fraud, but it did not apportion this amount among the separate claims. *See infra* App. 89. Although the district court found all but

one of E&R's fraud claims legally insufficient to support a judgment, it nonetheless included the entire $16,500,000 in punitive damages in the judgment. The court of appeals by its Judgment Order affirmed both the holding of no liability on most of the fraud claims and the entire punitive damage award. This affirmance of the punitive damage award, in effect allocating the entire award to only one of the multiple and distinct fraud claims E&R argued to the jury in connection with punitive damages, is improper as a matter of federal law and is in conflict with the decisions of the Second, Fourth and Eleventh Circuits.

Up to the decision of the Third Circuit in this case, the courts of appeals that had faced the issue had been uniform in concluding that where a general award of punitive damages is based upon more than one cause of action, one of which is reversed, the punitive damage award must be set aside. *See Murphy Door Bed Co. v. Interior Sleep Sys.*, 874 F.2d 95, 104 (2d Cir. 1989); *Litman v. Massachusetts Mut. Life Ins. Co.*, 739 F.2d 1549, 1562 (11th Cir. 1984); *Barnes Group, Inc. v. C & C Prods., Inc.*, 716 F.2d 1023, 1034 (4th Cir. 1983). In *Litman*, the plaintiff obtained an award of punitive damages based on two claims of slander. On appeal, the Eleventh Circuit reversed judgment on one of the two claims. In light of that reversal, the Eleventh Circuit remanded the punitive damage issue to the trial court for a new trial, stating that "[t]his result is [u]navoidable in light of the fact that the jury's $250,000 punitive damage award was made in response to a single question on the special verdict form." 739 F.2d at 1562. Indeed, because punitive damages are awarded based upon a theory that outrageous conduct should be

punished, the court held that the punitive damage award could not be sustained "based partly on the perceived outrageousness of that [nonslanderous] statement." *Id.* *See also Barnes Group*, 716 F.2d at 1034 ("because the punitive damage award hinges on the liability findings that we reverse in part, we must remand on the issue of punitive damages").

Similarly, the plaintiff in *Murphy Door* obtained an award of punitive damages based on claims of trademark infringement and unfair competition. In reversing the liability finding on the trademark claim, the Second Circuit held that the award of punitive damages must be remanded because "we are unable to determine what fraction of the punitive damages award, if any, is attributable to unfair competition." 874 F.2d at 104.

This same principle has been recognized and applied by the federal courts where a general award of actual damages is based on two or more causes of action, one of which has been determined not to state a claim. In such instances, the decision on what portion of the general damage award may be attributable to a claim that has been reversed has uniformly been held to require a new trial. *See, e.g., United New York & New Jersey Sandy Hook Pilot Ass'n. v. Halecki*, 358 U.S. 613, 619 (1959); *Neubauer v. City of McAllen*, 766 F.2d 1567, 1575-77 (5th Cir. 1985); *Lyle v. Bentley*, 406 F.2d 325, 327-28 (5th Cir. 1969); *Mosley v. CIA. MAR. ADRA, S.A.*, 314 F.2d 223, 226-27 (2d Cir.), *cert. denied*, 375 U.S. 835 (1963). The rationale for this principle, identical to that employed in the context of general awards of punitive damages, was aptly explained by the Second Circuit:

> Because the jury's verdict was a general one, it is not possible to know upon which of these two alternate grounds it predicated the finding . . . necessary to support [the plaintiff's] verdict against [the defendant]. In these circumstances, it is the duty of an appellate court to examine the adequacy of both grounds. If one of the grounds is found adequate and the other inadequate as a matter of law, the judgment must necessarily be reversed since "there is no way to know that the invalid claim . . . was not the sole basis for the verdict."

Mosley, 314 F.2d at 226-27 (citations omitted). *Cf. Zant v. Stephens*, 462 U.S. 862 (1983) ("One rule derived from the *Stromberg* case is that a general verdict must be set aside if the jury was instructed that it could rely on any of two or more independent grounds, and one of those grounds is insufficient, because the verdict may have rested exclusively on the insufficient ground."); *Stromberg v. California*, 283 U.S. 359, 370 (1931).

In this case, the punitive damage award was based on multiple claims of fraud, including at least one before and one after the leveraged buy-out, *see infra* App. 46, and it was made in response to a single question in the jury's interrogatories. *Id.* at 89. These fraud claims involved separate and distinct activities on the part of Swarovski – activities ranging from an allegedly insincere promise of exclusivity, which induced plaintiff to enter the contract, to a variety of alleged post-contract frauds, including Swarovski's failure to manufacture certain Disney figurines and the withdrawal of E&R's right to use the Swarovski name in marketing Crystal Signatures. Tort liability was upheld only on the fraudulent inducement

claim; nevertheless, the district court upheld the entire punitive damage award relying explicitly on actions, like alleged improper competition and breach of contract, that could not have been part of the sole remaining fraud claim. This decision and the action of the Third Circuit in affirming it are in conflict with the well-reasoned and established precedent of other United States Courts of Appeals, and both this conflict and the Third Circuit's error warrant the grant of a writ of certiorari and correction by this Court.

The principle adhered to by the other courts of appeals – that courts may not make a judicial allocation of a damage award – is of constitutional significance. "The Seventh Amendment directs that facts decided by a jury may not be 'reexamined' by a federal court, other than 'according to the rules of the common law' ". *Mattison v. Dallas Carrier Corp.*, 947 F.2d 95, 107 (4th Cir. 1991). Accordingly, although it is generally accepted that appellate courts have the power to order either a remittitur or a new trial, they do not have the power to modify an unliquidated damage award in a manner that usurps the power of the jury. *See Pincus v. Pabst Brewing Co.*, 752 F. Supp. 871, 874-75 (E.D. Wis. 1990) (citing *McKinnon v. City of Berwyn*, 750 F.2d 1383, 1392 (7th Cir. 1984)). *See also Browning-Ferris Indus. of Vermont, Inc. v. Kelco Disposal Inc.*, 492 U.S. 257, 278-79 (1989) ("In reviewing an award of punitive damages, the role of the District Court is to determine whether the jury's verdict is within the confines set by state law, and to determine, by reference to federal standards developed under Rule 59, whether a new trial or remittitur should be ordered."); *Dunn v. Owens-Corning Fiberglass*, 774 F. Supp. 929, 951 (D.V.I.

1991), *aff'd. in part, vacated in part, Dunn v. Hovic*, 1992 WL 228875, 1992 U.S. App. LEXIS 22749 (3d Cir.), *rehearing granted and opinion vacated* (October 8,1992) (recognizing that the court "cannot simply substitute its own judgment as to the appropriate amount of punitive damages without infringing upon plaintiff's constitutional right to a jury trial"); *Connell v. Sears, Roebuck & Co.*, 722 F.2d 1542, 1546 (Fed. Cir. 1983) (court may not substitute its judgment for that of the jury, because doing so would effectively be a denial of the right to a trial by jury).

In one particularly instructive case, the jury returned a verdict in which it found liability, on multiple theories, against a number of defendants, but returned a general verdict as to damages. *Rheuport v. Ferguson*, 819 F.2d 1459 (8th Cir. 1987). Thereafter, the district court granted judgment notwithstanding the verdict to several of the defendants and on several of the claims, and allocated the jury's general damage award among the remaining defendants and claims. The Eighth Circuit held that the district court's allocation of damages denied defendants their right to a trial by jury as to damages. *Id.* at 1464. The Eighth Circuit explained this holding as follows:

> The fundamental problem with the judgment as it stands before us is that we are unable to determine how much the jury awarded the plaintiffs on each of the several counts. We cannot say with assurance that the jury awarded any particular amount for the due process violation, intentional infliction of emotional distress, conversion, or destruction of chattels. The jury itself did not find each defendant liable on each of these claims. Moreover, the district court eliminated liability for some defendants on

> post-trial motions, thus exacerbating the need for a more explicit damage verdict.
>
> To summarize, damages in a jury trial must be found and apportioned by juries, not judges.

Id.

Petitioners are acutely aware of the power and the obligation of both the trial and appellate courts to review the punitive damage award in this case in accordance with the requirements of Pennsylvania law and the federal constitutional restrictions on punitive damage verdicts. *See Pacific Mut. Life Ins. Co. v. Haslip*, 111 S. Ct. 1032 (1991). Indeed, among the questions presented in this Petition are the Third Circuit's failures to satisfy its review obligations under this Court's decision in *Haslip*. However, the right and duty to review a punitive damage award, to require either remittitur or new trial in the event of excessiveness, and to render judgment for the defendant in the event of a want of substantial evidence, does not carry with it the power to function as the jury and allocate the punitive damages among causes of action, purporting, in effect, to read the jury's collective mind. It has been recognized that "[a]n assessment by a jury of the amount of punitive damages is an inherent and fundamental element of the common-law right to trial by jury. Therefore, . . . the seventh amendment guarantees the right to a jury determination of the amount of punitive damages. . . . " *Defender Indus., Inc. v. Northwestern Mut. Life Ins. Co.*, 938 F.2d 502, 507 (4th Cir. 1991). Accordingly, by determining that the entire punitive damage award was premised on the sole affirmed claim of fraud, and was not in any way based on or related to activities going exclusively to the four other

claims of fraud that E&R argued to the jury, both the district court and Third Circuit improperly crossed into the realm of matters which are reserved for the jury, in violation of Swarovski's rights under the Seventh Amendment.

The issue of judicial allocation of a federal jury's general damage award is one of procedural fairness and the effect to be given to a federal judgment. As such, it is necessarily a question of federal law and state law is not controlling, even in those instances in which state law provides the other grounds of decision. *See Barnes Group*, 716 F.2d at 1034; *Williams v. Powers*, 135 F.2d 153, 156 (6th Cir. 1943). *Cf. Browning-Ferris*, 492 U.S. at 278-79 ("Federal law, however, will control on those issues involving the proper review of the jury award by a federal district court and court of appeals."); *Donovan v. Penn Shipping Co.*, 429 U.S. 648, 649-50 (1977) ("The proper role of the trial and appellate courts in the federal system in reviewing the size of jury verdicts is, however, a matter of federal law."). The Third Circuit's affirmance of the district court's judgment for punitive damages based at least in part on claims which have been held to state no cause of action is directly contrary to decisions of the Second, Fourth and Eleventh Circuits on a question of federal law, and is similarly contrary to the rule that is uniformly applied in the analogous situation of general awards of actual damages based on multiple causes of action. Consequently, the Court should grant review in this case to resolve the conflict among the Circuits.

B. The Third Circuit's Affirmance Of The $16,500,000 Punitive Damage Award Without Opinion Violates Swarovski's Procedural Due Process Rights.

This Court recently made clear that appellate courts reviewing judgments for punitive damages are constitutionally obligated to make an independent review of the punitive damage awards, both as to whether the evidence supports such an award in any amount, and if so, whether the amount awarded is greater than that reasonably necessary to punish and deter. *Haslip*, 111 S. Ct. at 1044-45. In *Haslip*, the Court emphasized that there were three vital layers of safeguards provided by Alabama's scheme for imposing punitive damages, one of which was appellate review pursuant to defined and specific criteria. *Id.* at 1043-46. As the Court observed, Alabama's scheme provided an additional and necessary check on the jury's and trial court's discretion on punitive damages by requiring the appellate court to undertake a comparative analysis of the award, and by thereafter requiring that court to apply "the detailed substantive standards it has developed for evaluating punitive awards." *Id.* at 1045. This review, the Court concluded, makes "certain that the punitive damages are reasonable in their amount and rational in light of their purpose to punish what has occurred and to deter its repetition." *Id.* In addition, Alabama's scheme further called for the appellate court to apply a defined set of criteria "for determining whether a punitive damage award is reasonably related to the goals of deterrence and retribution." *Id.* The Court concluded that "application of these standards . . . imposes a sufficiently definite and meaningful constraint

on the discretion of Alabama fact finders in awarding punitive damages."[3] *Id.*

In this case, the Third Circuit affirmed the entire $16,500,000 award of punitive damages without any written opinion or reasoned explanation of the punitive damage award. As Swarovski pointed out in its Petition for Rehearing and Rehearing In Banc, *see infra* App. 114-16, such an affirmance constituted a judicial abdication of the Third Circuit's obligation to review the punitive damage award, in violation of Swarovski's procedural due process rights. Contrary to the meaningful review conducted by the Alabama Supreme Court in *Haslip*, the Third Circuit in this case failed to articulate any rationale in support of the large award of punitive damages. Based on that failure, it is simply impossible to determine whether the Third Circuit conducted an appropriate review of the punitive damage award, the standard under which that review was conducted[4], and the basis for the conclusions reached by the Third Circuit. This failure undercuts the

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[3] Through application of the factors adopted by the Alabama Supreme Court, the Court concluded that "Alabama plaintiffs do not enjoy a windfall because they have the good fortune to have a defendant with a deep pocket." *Id.* at 1045. In stark contrast, the jury in this case was permitted to hear evidence on Swarovski's net wealth. Indeed, in justifying the award of punitive damages in this case, the district court gives great import to the "extreme wealth of defendants (far in excess of the amount stipulated)." *See infra* App. 46.

[4] The standard of review of punitive damages on the common law claims is provided by the law of Pennsylvania, to the extent it comports with and satisfies the requirements of due process.

very legitimacy of a punitive damage award, the constitutionality of which the Court has explicitly conditioned on appropriate and meaningful appellate review.[5]

Petitioners recognize the time constraints and demands that the federal and state judiciaries are subject to, and the necessity of deciding certain appropriate cases without a written opinion. It is, however, critical to determine under what circumstances those conditions occur. The reasons for limiting the circumstances in which a court of appeals will dispense with a written opinion were well-explained when that procedure was first being implemented:

> Opinions are to serve a number of purposes at least two of which are highly significant. One is that an articulated discussion of the factors, legal, factual or both, which lead the Court to one rather than to another result, gives strength to the system, and reduces, if not eliminates, the easy temptation or tendency to ill-considered or even arbitrary action by those having the awesome power of almost final review. . . .
>
> * * *
>
> The Court recognizes that it must – the word is must – never apply the Rule to avoid making a difficult or troublesome decision or to conceal divisive or disturbing issues. This means that

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[5] Indeed, to the extent that punitive damages are in large part awarded to deter future conduct, *see, e.g., Haslip*, 111 S. Ct. at 1044, the absence of any written explanation as to why punitive damages were warranted in this case further undercuts the rationale supporting the award of punitive damages, and thus their legitimacy.

> while [summary affirmance] should make a real contribution toward the goal of avoiding delays which can often amount to a denial of justice, it must be sparingly used.

National Labor Relations Bd. v. Amalgamated Clothing Workers, 430 F.2d 966, 972 (5th Cir. 1970) (Brown, C.J.).

The Fifth Circuit's admonition necessarily suggests that the procedure for affirming without an opinion will be confined to cases involving well-established legal propositions and/or involve minor legal consequences to the litigants. It is inappropriate, under *Haslip*, to utilize this procedure in a litigation in which the jury has awarded $16,500,000 in punitive damages, the constitutionality of which is dependent upon appropriate appellate review.[6] Accordingly, this Court should grant certiorari here in order to clarify and define the nature of

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[6] The notion that a court should be obligated to provide a written articulation of reasons in support of its decision is neither novel, nor is it onerous in the context of punitive damage awards. The Court has recognized that punitive damage awards are quasi-criminal in nature. *See Haslip*, 111 S. Ct. at 1044 (citing *Smith v. Wade*, 461 U.S. 30, 59 (1983) (Rehnquist, J., dissenting)). Punitive damages are imposed for purposes of retribution and deterrence, two functions also served by criminal penalties.

In the analogous context of imposing criminal penalties, the federal courts must provide an articulation of "reasons for [the] imposition of the particular sentence." 18 U.S.C. § 3553(c). Indeed, the more extreme the penalty, the greater the required degree of specificity. *See, e.g., United States v. Beaulieu*, 900 F.2d 1537, 1540-41 (10th Cir.), *cert. denied*, 497 U.S. 1009 (1990); *United States v. Terry*, 916 F.2d 157, 160-61 (4th Cir. 1990); *United States v. Delvecchio*, 920 F.2d 810, 813-14 (11th Cir. 1991); *United States v. Sanchez*, 933 F.2d 742, 745 (9th Cir. 1990); *United States v. Himsel*, 951 F.2d 144, 147 (7th Cir. 1991).

the appellate review that is required when a court of appeals considers an award of punitive damages.

C. The Excessive And Disproportionate Nature Of The $16,500,000 Punitive Damage Award Violates Swarovski's Substantive Due Process Rights.

By failing to articulate the basis for the punitive damage award, the Third Circuit has hidden significant legal deficiencies with the award that demonstrate that it is unconstitutionally excessive, disproportionate to the nature of Swarovski's conduct, and in violation of Swarovski's substantive due process rights. The sole grounds which the district court listed in support of its requisite finding of outrageous conduct on the part of Swarovski which might justify an award of punitive damages were that Swarovski's witnesses were arrogant and that the jury found against Swarovski on all counts. App. 46. Neither "fact" is a sufficient basis on which to support the award of $16,500,000 in punitive damages. Any arrogance on the part of Swarovski's witnesses is completely irrelevant to an award of punitive damages. Punitive damages can only be awarded based on tortious conduct of a defendant, not on the personality traits of its witnesses at trial. However desirable it might be to deter the "arrogance" of witnesses in the courtroom, that is not a matter committed to the realm of punitive damages under *Haslip* or any state law of damages, including that of Pennsylvania. Similarly, a finding of liability, even on all counts, is not evidence of outrageous conduct. *See Tunis Bros. Co. v. Ford Motor Co.*, 952 F.2d 715, 741 (3d Cir. 1991), *cert. denied*, 112 S. Ct. 3034 (1992); *Smith v. Renaut*, 564 A.2d 188, 193 (Pa. 1989). Rather, there must be acts of

malice, vindictiveness or wholly wanton disregard of the rights of others, in addition to that which supported the finding of fraud liability and the award of compensatory damages, in order to support an award of punitive damages. *Tunis Bros.*, 952 F.2d at 741.

These deficiencies in the district court's justifications for the punitive damage award are in this case exacerbated by the Third Circuit's failure to articulate its review of the punitive damage award. No court in this matter has ever given a viable reason to justify the award of $16,500,000 in punitive damages. Clearly, a finding of fraud without a sufficient basis for a finding of outrageous conduct does not merit an award of punitive damages. *See Hughes v. Consol-Pennsylvania Coal Co.*, 945 F.2d 594, 616 (3d Cir. 1991), *cert. denied*, 112 S. Ct. 2300 (1992).

In this regard, two points are particularly important. First, this case arose out of a business tort, not involving loss of life or limb or threat to public health and safety. *Cf. Alexander & Alexander, Inc. v. B. Dixon Evander & Assocs.*, 596 A.2d 687, 719 (Md. Ct. Spec. App. 1991), *cert. denied*, 605 A.2d 137 (Md. 1992) ("This was, at bottom, a commercial dispute between two business competitors."); *Medical Mut. Liab. Ins. Soc'y v. B. Dixon Evander & Assocs.*, 609 A.2d 353, 369 (Md. Ct. Spec. App.), *cert. denied*, 614 A.2d 973 (1992) (holding that the "commercial dispute that triggered the awards of punitive damages was not 'very high on the scale of reprehensibility' "). Rather, the award of punitive damages in this case is premised solely on a claim of fraudulent inducement into a contract – and E&R has already been awarded future lost profits of $25,000,000 on the contract. To nearly double that already staggering sum serves no legitimate purpose of punitive

damages and grants to E&R a "windfall" because it had "the good fortune to have a defendant with a deep pocket." *Haslip*, 111 S. Ct. at 1045.[7]

In addition, in the face of a $200,000,000 stipulated net worth for Swarovski, the district court upheld a punitive damage award amounting to 8.25% of that figure, a number far in excess of the usual court approved percentage. *See Cash v. Beltmann N. Am. Co.*, 900 F.2d 109, 111 n.3 (7th Cir. 1990) ("[A] typical ratio for a punitive damages award to a defendant's net worth [is] around one percent."). In entering judgment on this award, the district court improperly relied on an unsupported "hunch" that the Swarovski's "extreme wealth" was "far in excess of the amount stipulated." *See infra* App. 46.

The holding in *Haslip*, requiring that all courts must give serious content and consideration to the Due Process Clause when reviewing and approving punitive damage awards has not been embraced by all the courts bound to apply its teachings. This failure is vividly demonstrated by the Third Circuit's affirmance of the $16.5 million punitive damage award in this case without acknowledging either the standards for review of punitive damage awards under Pennsylvania law or the constraints of due process. In apparent recognition of the failure of many state and lower federal courts to harmonize their practices on the review of punitive damage awards with the teaching of *Haslip* – a circumstance of which this case is an additional example – this Court took for review this

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[7] E&R's actual out-of-pocket damages were found to be only $850,000, slightly more than one-twentieth (1/20) of the punitive damage award.

term the questions presented in *TXO Production Corp. v. Alliance Resources Corp., et al.*, No. 92-479. Presumably, by the time this Petition is read, the Court's Opinion in *TXO* will have been announced. Regardless of the fate of the $10,000,000 punitive damage award at issue in *TXO*, the summary affirmance by the Third Circuit in this case of a fortune[8] in punitive damages, without any articulation of the grounds therefor, simply cannot be sanctioned as part of a constitutionally acceptable punitive damage scheme, if *Haslip* is to have any meaning at all. Accordingly, the Court should grant review in this case to make plain that *Haslip* and the Due Process Clause require genuine constraints on jury and judicial discretion and that meaningful and articulated appellate review, with defined criteria, is an important component of any constitutionally sound punitive damage scheme.

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[8] Questions of ratio should not blind the courts to an appreciation of the shocking absolute size of a punitive damage award. Indeed, where a plaintiff in a purely commercial dispute is already receiving monetary compensation for a monetary loss and, as here, the defendant did not unjustly enrich itself on the transaction, so that a punitive damage award could serve as a form of disgorgement, a large punitive damage award in addition to a large award of compensatory damages would appear to advance none of the legitimate purposes of punitive damages, but merely provide a jackpot for the plaintiff.

CONCLUSION

For the reasons set out above, the petition for writ of certiorari should be granted.

Respectfully submitted,

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Counsel for Petitioners

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June 23, 1993

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 92-1723, 92-1746

EBELING & REUSS, LTD.
t/a EBELING & REUSS COMPANY,

Appellant in 92-1723

v.

SWAROVSKI INTERNATIONAL TRADING CORPORATION A.G.; D. SWAROVSKI & CO.; SWAROVSKI AMERICA LIMITED; SWAROVSKI AKTIENGESELLSCHAFT

Appellants in 92-1746

Appeal from the United States District Court
for the Eastern District of Pennsylvania
D.C. Civil Docket No. 88-04878
(District Judge: Honorable Norma L. Shapiro)

Argued: March 16, 1993
Before: STAPLETON, ROTH and LEWIS, *Circuit Judges*

JUDGMENT ORDER

After consideration of all contentions raised by appellants,

IT IS ADJUDGED AND ORDERED that the judgment of the district court be and is hereby affirmed.

Each appellant shall bear the costs of its own appeal.

BY THE COURT.

/s/ Illegible
Circuit Judge

Attest:

/s/ P. Douglas Sisk
P. Douglas Sisk, Clerk

DATED: APR 7 1993

UNITED STATES COURT OF APPEALS
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EBELING & REUSS, LTD.
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Appellant in 92-1723

v.

SWAROVSKI INTERNATIONAL TRADING CORPORATION A.G.; D. SWAROVSKI & CO.; SWAROVSKI AMERICA LIMITED; SWAROVSKI AKTIENGESELLSCHAFT

Appellants in 92-1746

Before: SLOVITER, *Chief Judge*, BECKER, STAPLETON, MANSMANN, GREENBERG, HUTCHINSON, SCIRICA, COWEN, NYGAARD, ALITO, ROTH and LEWIS, *Circuit Judges*

SUR PETITION FOR REHEARING

The petition for rehearing filed by appellants in 92-1746 in the above-entitled case having been submitted to the judges who participated in the decision of this court and to all other available circuit judges of the circuit in regular, active service, and no judge who concurred in the decision having asked for rehearing, and a majority of the circuit judges of the circuit in regular active service

not having voted for rehearing by the court *in banc,* the petition for rehearing is hereby denied.

BY THE COURT.

/s/ Illegible
Circuit Judge

DATED: MAY 17 1993

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

EBELING & REUSS, LTD. t/a EBELING & REUSS COMPANY,	:	CIVIL ACTION (Filed Aug. 24, 1992)
v.	:	
SWAROVSKI INTERNATIONAL TRADING CORPORATION, A.G., individually and d/b/a D. SWAROVSKI & CO. and SWAROVSKI AMERICA LIMITED and SWAROVSKI AKTIENGELSELLSCHAFT	:	NO. 88-4878

MEMORANDUM AND ORDER

NORMA L. SHAPIRO, J. AUGUST 24, 1992

I. INTRODUCTION

Plaintiff Ebeling & Reuss, Ltd. ("E&R, Ltd.") was awarded a jury verdict in excess of $55 million against defendants Swarovski International Trading Corporation, A.G., individually, and doing business as D. Swarovski & Co., Swarovski America Limited, and Swarovski Aktiengelsellschaft (collectively referred to as "Swarovski"), for breach of contract, promissory estoppel, tortious interference with contract, fraud, civil conspiracy, trademark infringement, unfair competition, and misappropriation of a trade secret. Pending are both parties' numerous post trial motions for judgment notwithstanding the verdict, to alter or amend the verdict, new

trial, and additur as well as defendants' motion for disqualification and plaintiff's motions for contempt and attorneys' fees.

Jurisdiction arises under 28 U.S.C. § 1332; plaintiff Ebeling & Reuss, Ltd. is a Pennsylvania corporation with its principal place of business in Devon, Pennsylvania; defendants Swarovski International Trading Corporation, A.G., D. Swarovski & Co., and Swarovski Aktiengelsellschaft are incorporated under the laws of Switzerland, Austria, and Liechtenstein respectively; defendant Swarovski America Limited is a corporation incorporated under the laws of Rhode Island with its principal place of business in Cranston, Rhode Island. The parties agree that Pennsylvania law applies.

In response to special interrogatories,[1] the jury found in favor of Ebeling & Reuss, Ltd. on all claims. On the E&R, Ltd. claims for breach of contract, tortious interference with contract, promissory estoppel, and fraud, the jury awarded $33,850,000 in compensatory damages ($850,000 in actual damages, $25 million in lost profits, and $8 million in harm to reputation) – and $16,500,000 in punitive damages. On the E&R, Ltd. trademark infringement and unfair competition claims, the jury awarded $0 in compensatory damages but $2,500,000 in punitive

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[1] The special interrogatories answered by the jury are attached. The interrogatories answered on liability for contract, promissory estoppel, tortious interference with contract, fraud, and conspiracy are attached as Appendix A. The interrogatories on damages for those claims are attached as Appendix B. The interrogatories on trademark, unfair competition, and misappropriation of trade secret are attached as Appendix C.

damages. On the E&R, Ltd. claim for misappropriation of a trade secret, the jury awarded $291,364 in compensatory damages and $2,500,000 in punitive damages. The court entered judgment in favor of E&R, Ltd. in the amount of $55,641,364.

Defendants' motions for judgment notwithstanding the verdict and to alter or amend the verdict will be granted in part and denied in part. Defendants' motion for new trial will be denied. Plaintiff's motions for new trial, to amend the verdict, for additur, and for attorneys' fees will be denied. The court will reserve ruling on plaintiff's motions for contempt and attorneys' fees on the contempt claim to allow plaintiff to inform the court whether it wishes to pursue those motions.

II. FACTUAL BACKGROUND

This action arose out of the Swarovski defendants' alleged repudiation of an agreement to permit Ebeling & Reuss Company to market and distribute miniature, injection molded, full lead, crystal figurines manufactured by D. Swarovski & Co. The relationship between Ebeling & Reuss and D. Swarovski began in 1986 when Ebeling & Reuss Company ("E&R Co.") was still an unincorporated division of Alco Standard Corporation. The Swarovski business entities are all related corporations owned by the Swarovski family and managed by a joint board called the Beirat.

Helmut Swarovski, a Beirat member, invented a new technology for producing injection molded crystal figurines. Helmut Swarovski, working with Peter Yenawine, a designer and long time friend, and Yenawine's company,

Pynn Corporation, designed figurines for manufacture with this new technology.

Early in 1986, Peter Yenawine introduced E&R Co. as a potential distributor for these injection molded crystal figurines to Helmut Swarovski. Swarovski and E&R Co. entered into a distribution agreement through a series of written and oral communications. Swarovski first dealt with Allen Goeldner, President of E&R Co., and thereafter with Michael Russo, initially Vice President, then President, of E&R Co. and finally President and part owner of E&R, Ltd. Most of the early dealings between E&R Co. and Swarovski were conducted through Peter Yenawine and his attorney, Stephen Palmer. In 1987, Ebeling & Reuss, Co. and Swarovski negotiated an integrated written contract to formalize their relationship; the contract was drafted but never signed by Swarovski.

Ebeling & Reuss, Co. marketed and distributed the line under its registered trademark, "Crystal Signatures," in packaging provided by Swarovski with the legend, "Crafted by D. Swarovski & Co., Wattens." In February, 1987, Lawrence Metcalfe, President of Swarovski America Limited ("SAL"), mailed a letter to SAL customers who sold Silver Crystal, a line of faceted crystal figurines also manufactured by Swarovski; his letter stated that Ebeling & Reuss' Crystal Signatures had no connection with SAL, and suggested that Ebeling & Reuss was not authorized to use the "Swarovski" name. However, the D. Swarovski & Co. business relationship with E&R Co., and then E&R, Ltd., continued into 1988; E&R Co. placed orders with Swarovski for six Yenawine designed figurine series and negotiated a license agreement with Walt Disney & Co. to distribute injection molded Disney figurines.

In late 1987, Alco Standard had decided to sell its E&R division. Russo and other investors formed E&R, Ltd. to purchase E&R Co. E&R, Ltd. purchased E&R Co. from Alco Standard on March 31, 1988; the agreement of sale assigned the Disney license agreement and the Swarovski agreement concerning Crystal Signatures to E&R, Ltd.[2] However, on June 1, 1988, SAL's attorney wrote Ebeling & Reuss, Ltd. that E&R, Ltd. could not ship Swarovski product or use the Swarovski name in any way until the parties reached a mutually satisfactory written agreement. In the Fall of 1988, Zales, an SAL subsidiary, began selling Swarovski injection molded crystal figurines as Zales' "Crystal Collectibles."

On June 20, 1988, E&R, Ltd. filed this Complaint and moved for a preliminary injunction. Hearings on the motion were held on July 14, 26, and 27, 1988. On July 29, 1988, the court ordered defendants to undertake, as expeditiously as possible, all necessary steps to provide plaintiff with 24 first quality samples of eight Crystal Signatures Disney character figurines, with a base for

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[2] The agreement states in pertinent part:

2. Alco hereby sets over, transfers, assigns, sells and otherwise conveys fully to E&R, free and clear of all liens and encumbrances;

* * *

g. Any and all rights benefits and obligations to contracts to which Alco and/or E&R Co. is a party concerning the operations of E&R Co. including but not limited to that certain license agreement with Walt Disney Company, and that certain agreement with D. Swarovski and Company concerning Crystal Signatures.

each, by August 30, 1988. The court denied defendants' motion for a stay pending appeal or, in the alternative, to modify the preliminary injunction of July 29, 1988. On December 30, 1988, the Court of Appeals affirmed this court's Order granting a preliminary injunction. *Ebeling & Reuss, Ltd. v. Swarovski Intern. Trading Corp.*, 866 F.2d 1409 (3d Cir. 1988).

Defendants failed to produce the Disney figurines for E&R, Ltd. by August 30, 1988 in violation of the preliminary injunction. A hearing on plaintiff's motion to hold defendants in contempt was held on September 14, 15 and October 6, 1988. The court deferred decision on the motion for contempt until after trial on the merits. New counsel for defendants filed a motion for disqualification of this judge that was denied on January 30, 1990. Defendants' motion for summary judgment, filed January 18, 1990, was denied on June 4, 1990 and a three week jury trial, concluded June 21, 1990, resulted in a verdict for plaintiff on all counts.

Pursuant to Federal Rule of Civil Procedure 50, defendants filed post trial motions for judgment notwithstanding the verdict, to alter or amend the verdict and for a new trial. Plaintiff filed motions for attorneys' fees, a motion to amend the verdict, a motion for additur, and a conditional motion for a new trial.[3]

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[3] The court delayed ruling on the outstanding motions for some time because the parties were engaged in settlement negotiations.

III. DEFENDANTS' MOTIONS

A. JUDGMENT NOTWITHSTANDING THE VERDICT

A judgment notwithstanding the verdict is appropriate only where, as a matter of law, the jury's verdict was not supported by sufficient evidence to allow reasonable jurors to arrive at the verdict. *Link v. Mercedes-Benz of North America*, 788 F.2d 918, 921 (3d Cir. 1986). *Berndt v. Kaiser Aluminum & Chemical Sales, Inc.*, 789 F.2d 253 (3d Cir. 1986). To grant judgment notwithstanding the verdict, the court must find as a matter of law that "the record is critically deficient of the minimum quantity of evidence from which the jury must reasonably afford relief." *Simone v. Golden Nugget Hotel and Casino*, 844 F.2d 1031, 1034 (3d Cir. 1988). The party prevailing at trial is entitled to the benefit of all reasonable inferences that can be drawn from the evidence in determining whether there is any rational basis for the verdict. *Bhaya v. Westinghouse Electric Corp.*, 832 F.2d 258, 259 (3d Cir. 1987), *cert. denied*, 468 U.S. 1004 (1989). Therefore, this court must determine only whether the evidence and the justifiable inferences in favor of the prevailing party afford any rational basis for the verdict.

Defendants' reasons why judgment notwithstanding the verdict should be granted are considered below.

1. Contract

a. Contract – E&R, a Division of Alco Standard, and Swarovski

Defendants concede the existence of a contract between Swarovski and E&R Co., an unincorporated division of Alco Standard Corp., to distribute Crystal Signatures. However, defendants contended the contract was limited to those Yenawine-designed crystal figurines for which E&R Co. submitted purchase orders to Swarovski. E&R Co.'s successor and assignee, E&R, Ltd. claimed at trial that the contract was for the entire "product line" and that Swarovski could not compete with E&R Co. directly or indirectly in the North American market for injection molded crystal collectible figurines for the life of the products.

This issue was presented to the jury (Charge, N.T. 6/15/90 at 102), and its answers to the contract interrogatories (A)(3) and (A)(6) and damage interrogatory (1) make it clear that the jury found E&R Co. had the exclusive contractual right to market the entire product line for the life of the products.

Defendants argue that the jury's determination should be set aside as against the weight of the evidence because Yenawine's trial testimony and his memorandum of May 31, 1986 (P-26) clearly show that the Swarovski-E&R Co. agreement did not preclude Swarovski's entering the market with its own line of injection molded figurines. Yenawine's memorandum of May 31, 1986, suggested arguments Helmut Swarovski should make to the Beirat to get the Beirat's approval of E&R Co.'s use of the Swarovski name on Crystal Signatures packaging. One of

Yenawine's suggested arguments was that E&R Co. could test the market for Swarovski and create recognition of the Swarovski name in the smooth crystal figurines market. If E&R Co. knew of Swarovski's future intention to introduce competing figurines, it would rebut E&R Co.'s contention that it was offered exclusive rights to the entire product line for the life of the product.

However, no evidence was introduced that anyone at E&R Co. saw Yenawine's memorandum prior to this litigation. Yenawine did not recall whether or not he showed it to anyone from E&R Co. Russo testified he never would have entered into a distributorship agreement with Swarovski or expended so much money in advertising and promoting the Crystal Signatures line if he had known of Swarovski's intention to use E&R Co. merely to test the market. The jury could reasonably infer that neither Yenawine nor Swarovski communicated the contents of this memo to E&R Co.

The court instructed the jury to consider the writings and the conduct of the parties to determine the terms of the contract. The jury could have rationally determined from all the evidence that a contract existed between the parties. Such evidence included but was not limited to: a March 20, 1986 telex from Kurt Mignon to Stephen Palmer (P-12); a copy of the May 26, 1986 Beirat minute (P-22); the June 3, 1986 Beirat minute (P-27); Gernot Langes-Swarovski's June 12, 1986 memo to file (P-32); a July 22, 1986 telex from Mignon to Yenawine (P-44); a letter agreement relating to mold charges (P-103); and Ebeling & Reuss, Co. purchase orders (P-42, 249, and 264). The jury's determination that E&R Co. had the

exclusive right to market the entire product line for the life of the products had support in the evidence and should not be set aside.

b. Pre-Assignment Breach

E&R, Ltd. claimed defendants breached the Crystal Signatures contract with E&R Co. prior to March 31, 1988 by delivering late, revoking E&R Co.'s right to use the Swarovski name, and marketing a competing line. Defendants contended that E&R Co. agreed to modified delivery schedules, never stopped using the Swarovski name, and was not told to do so until June 1, 1988. Defendants also contended that even if there were a contract, the breach, if any, occurred only after incorporation of E&R, Ltd. (on March 31, 1988) because Swarovski did not introduce the Zales' Crystal Collectibles injection molded figurines until Fall, 1988. However, the jury found there was an enforceable contract (Appendix A, Contract Interrogatory 1) and that it was breached prior to March 31, 1988 (Appendix A, Contract Interrogatory 2).

Prior to March 31, 1988, the Beirat had met on more than one occasion when it decided not to allow E&R Co. to use the Swarovksi name. However, Swarovski negotiated with E&R Co. after the Beirat made that decision in an attempt to get E&R Co. to agree not to use the name. When E&R Co. would not agree to stop using the Swarovski name that was already on its new packaging material in accordance with the contract, Swarovski attempted to force E&R Co. to stop distributing Crystal Signatures by raising the price of the figurines and failing to confirm orders. E&R, Ltd. introduced evidence that

Swarovski was planning and marketing the competing Zales line as early as Summer, 1987, although the Zales line was not actually manufactured until after March 31, 1988. The evidence was sufficient for the jury to find Swarovski breached its contract with E&R Co. prior to March 31, 1988. These jury findings should not be set aside.

c. Assignment of Chose in Action

The court instructed the jury it could find that Alco Standard's assignment to E&R, Ltd. of "rights, benefits and obligations" under the Swarovski agreement transferred the right to sue for any breach occurring prior to the assignment, whether or not the contract itself was assignable. Defendants claim that instruction was in error.

Defendants contend that Alco Standard's cause of action could not be assigned to E&R, Ltd. unless the contract itself was assignable. However, the general rule is that any cause or right of action that would survive the death of the assignor may be assigned. *See* 3 *Penna. Law Encyclopedia,* Assignments §7.

Defendants claim that the cause of action was not in fact assigned since there was no reference to an "assignment of a chose in action" in the contract between Alco Standard and E&R, Ltd. However, the jury could reasonably have found that the broad language assigning all rights, benefits and obligations under the contract included any cause of action Alco Standard may have had

against Swarovski. Defendants point out that the exceptions Alco withdrew from assignment to E&R, Ltd. included certain causes of action Alco Standard was then litigating. That supports E&R, Ltd.'s claim that Alco Standard did not exclude its claims against Swarovski in its broad general assignment of all rights, benefits, and obligations to E&R, Ltd. Alco Standard's cause of action was clearly assignable.

d. Contract Assignment or Termination by Swarovski

The jury found that Swarovski had a right to terminate the contract with E&R Co. when E&R Co., an unincorporated division of Alco Standard, was sold to newly formed E&R, Ltd. on March 31, 1988, but Swarovski waived that right. (Appendix A, Contract Interrogatories 4&5). Swarovski contends that it did not waive the right because Swarovski communicated to E&R, Ltd. its refusal to execute the written contract negotiated in 1987 with Alco Standard on May 9, 1988 and Swarovski told E&R, Ltd. it could no longer use the Swarovski name on June 1, 1988. However, there was also evidence that during meetings in May, 1988, Swarovski was ready to produce the Disney figurines for E&R, Ltd. and asked E&R, Ltd. to approve samples. Swarovski and E&R, Ltd. were continuing to negotiate a written contract at that time.

The jury could reasonably have found that Swarovski's refusal to sign the written contract was simply a refusal to modify the existing agreement. The June 1, 1988 letter did not state that Swarovski was terminating its contract with E&R, Ltd. or that no agreement

existed; Swarovski said it was revoking the right to use its name in connection with Crystal Signatures figurines not that it was terminating the agreement to produce figurines for E&R, Ltd. There was nothing inconsistent in plaintiff's argument that revocation of the right to use the Swarovski name was a breach of the contract but not its termination. E&R, Ltd. introduced evidence that Swarovski continued to behave as though the original agreement remained in effect. The jury was entitled to find plaintiff's evidence more persuasive than that of defendants.

2. Tortious interference

Pennsylvania recognizes the torts of tortious interference with existing contractual rights and tortious interference with prospective contractual relations. *See U.S. Healthcare v. Blue Cross of Greater Philadelphia,* 898 F.2d 914 (3d Cir.) *cert. denied* 111 S.Ct. 58 (1990). Plaintiff claimed interference with two existing contracts: 1) Swarovski's failure to produce the Disney figurines as it had agreed interfered with the Disney-E&R licensing agreement; 2) SAL interfered with E&R Co.'s contract with the other defendants. Plaintiff also claimed interference with prospective contracts: the SAL letter Metcalfe sent in February, 1987, allegedly interfered with a series of prospective contracts because E&R Co. customers stopped ordering Crystal Signatures as a consequence of the letter.

a. Interference with Existing Contracts

Pennsylvania has adopted the test set forth in the Restatement (Second) of Torts for determining liability for interference with existing contractual rights:

> One who intentionally and improperly interferes with the performance of a contract (except a contract to marry) between another and a third person by inducing or otherwise causing the third person not to perform the contract, is subject to liability to the other for the pecuniary loss resulting to the other from the third person's failure to perform the contract.

U.S. Healthcare, 898 F.2d at 925 (quoting Restatement (Second) of Torts § 766 (Tent. Draft No. 23, 1977) (citations omitted). The existing contract right must first be established. *Id.*

(1) SAL interference with E&R Co.'s contract with the other Swarovski defendants

The jury found an exclusive contract existed between E&R Co. (assigned to E&R, Ltd) and Swarovski. As stated in the discussion of the contract claim, that was a reasonable finding based on the evidence.

Plaintiff introduced evidence that SAL was strongly opposed to E&R Co.'s use of the Swarovski name on its packaging and put pressure on the Beirat to revoke E&R Co.'s right to use the Swarovski name. The Beirat then resolved to get E&R Co. to stop using the Swarovski name one way or another. Martin Halusa, President of SAL, proposed several possible ways to get E&R Co. to

relinquish the right to use the Swarovski name. The Beirat began negotiating with E&R Co. concerning disuse of the Swarovski name. Ultimately, the June 1, 1988 letter revoking E&R, Ltd.'s right to use the Swarovski name was sent; this was a breach of the contract.

A person or entity cannot be held liable for tortious interference with a contract to which it was a party. *See Abel v. American Art Analog, Inc.*, 838 F.2d 691, 698 (3d Cir. 1988); *Michelson v. Exxon Research and Eng'g Co.*, 808 F.2d 1005, 1007-08 (3d Cir. 1987). Neither can an agent acting on behalf of its principal be held liable for tortious interference with a contract to which its principal is a party. *See, e.g., Michelson*, 808 F.2d at 1007-08 (corporate employee acting in the scope of his employment cannot tortiously interfere with a contract to which the corporation is a party). Although the Swarovski entities were incorporated as separate companies, they were all controlled by the Beirat and acted as one entity. *See College Watercolor Group, Inc. v. William H. Newbauer, Inc.*, 360 A.2d 200, 207 (Pa. 1976) ("corporate veil is properly pierced whenever one in control of a corporation uses that control or corporate assets to further one's own personal interests"). Therefore, one member of the Swarovski group cannot be liable for tortious interference with a contract to which another Swarovski entity is a party. SAL's actions cannot be tortious interference with the Swarovski-E&R contract as a matter of law.

(2) Interference with Disney Licensing Agreement

The only post-March 31, 1988 conduct which plaintiff claims constituted tortious interference was Swarovski's failure to provide the Disney samples resulting in a breach of E&R, Ltd.'s agreement with Disney. The parties stipulated that the Disney agreement had been signed. The evidence of the existence of a contract with Disney was sufficient.

Helmut Swarovski and the Swarovski defendants knew of E&R, Ltd.'s licensing agreement with Disney. E&R, Ltd. informed Swarovski that the sample Disney figurines had to be ready for the Disney Expo in September, 1988. With knowledge that its actions would put the Disney agreement in jeopardy, Swarovski failed to work on the Disney figurines during the Summer of 1988 in violation of the July 29, 1988 court order requiring Swarovski to furnish samples to plaintiff by September, 1988. On August 4, 1988, Swarovski moved for a stay pending appeal or a modification of the order in the alternative on the ground of impossibility or inability to comply. Meanwhile, Swarovski was using its capacity for making injection molded crystal figurines to manufacture a competing Zales Crystal Collectibles line of figurines.

This conduct was a breach of contract and in contempt of court but it was not tortious interference. Defendants did not induce or otherwise cause Disney (the third person) to breach its agreement with E&R, Ltd.; defendants' breach of contract prevented E&R, Ltd. from performing the Disney agreement. Plaintiff may recover

consequential damages for that breach but plaintiff cannot recover tort damages.

b. Interference with Prospective Contracts

Pennsylvania law recognizes a cause of action for tortious interference with a prospective contract. *See Thompson Coal Co. v. Pike Coal Co.*, 412 A.2d 466 (Pa. 1979); *Glenn v. Point Park College*, 272 A.2d 895 (Pa. 1971). Plaintiff must prove a reasonable probability that the contract would have been executed. *Tose v. First Pennsylvania Bank*, 648 F.2d 879, 898 (3d Cir.), *cert. denied*, 454 U.S. 893 (1981); *General Sound Telephone Co. v. AT&T Communications*, 654 F. Supp. 1562, 1565 (E.D. Pa. 1987); *Thompson Coal*, 412 A.2d at 471; *Glenn*, 272 A.2d at 898-99. In *General Sound*, the district court held that testimony from the prospective contractee that he probably would have *considered* contracting with the plaintiff was insufficient. 654 F. Supp. at 1565. The court implied that testimony from the third party that he probably would have *contracted* with the plaintiff was required. *Id.*

Michael Russo, President of E&R, Ltd., testified that as a result of the Metcalfe letter, stating E&R Co. was not authorized to use Swarovski's name, retailers questioned E&R Co. salesmen about the authenticity of Crystal Signatures. Russo did not name particular retailers or offer documentary evidence of complaints resulting from the Metcalfe letter. Plaintiff relied on a drop in sales several months after the Metcalfe letter was sent to prove that the letter kept retailers from buying the Crystal Signatures line from doing so. This evidence as to prospective sales contracts was insufficient as a matter of law to establish a

reasonable probability that some retailers would have placed Crystal Signatures orders with E&R Co. Since this was the only evidence of pre-March 31, 1988 third party prospective contractual relations with which the Swarovski defendants allegedly interfered, the jury finding (C)(3) of tortious interference with prospective contractual relations cannot be sustained as a matter of law. *See* Appendix A.

3. Fraud

Plaintiff's principle claim of fraud was that Swarovski induced E&R Co. to enter into a contract to market, advertise, and sell Swarovski manufactured injection molded crystal figurines by representing that E&R Co.'s distributorship would be exclusive when Swarovski intended to capitalize on E&R Co.'s efforts and market and sell a competing line of figurines. Defendants contend that there is no evidence that any Swarovski entity intentionally made a false statement to either E&R Co. or E&R, Ltd. or failed to use reasonable care to inform E&R of anything the Swarovski defendants were under an affirmative duty to disclose.

To support a claim of fraud, a plaintiff must show: "(1) a misrepresentation; (2) a fraudulent utterance or nondisclosure; (3) an intention by the maker that the recipient will thereby be induced to act; (4) justifiable reliance by the recipient upon the misrepresentation; and (5) damage to the recipient as the proximate result." *Marian Bank v. Int'l Harvester Credit Corp.*, 550 F. Supp. 456, 461 (E.D. Pa. 1982); *Neuman v. Corn Exchange National Bank & Trust Co.*, 51 A.2d 759 (1947); *see also Sowell v.*

Butcher & Singer, Inc., 926 F.2d 289, 296 (3d Cir. 1991) (citations omitted).

a. Fraud on E&R Co.

Plaintiff claims defendants misrepresented to E&R Co. that they intended to give E&R Co. the exclusive distribution rights to the injection molded crystal figurine line. Defendants dispute that they made any misrepresentations to E&R Co. Defendants claim E&R Co. knew of the possibility that Swarovski would manufacture competing injection molded crystal figurines because Yenawine and Palmer knew of that possibility and Yenawine testified he would not have kept that information from E&R Co. But Yenawine testified he did not recall whether anyone from E&R Co. actually received that information. Although the jury could have inferred that E&R Co. knew Swarovski might later market a competing line, the jury did not have to reach that conclusion. Based on all the testimony, the jury could reasonably have found that E&R Co. did not know Swarovski intended to compete with Crystal Signatures at a later date. (Appendix A, Fraud Interrogatories (D)(1-4))

A breach of contract does not ordinarily give rise to tort liability. *See Iron Mountain Security Storage Corp. v. American Specialty Foods, Inc.*, 457 F. Supp. 1158, 1166 (E.D. Pa. 1987). However, a party can be liable for fraud if the party intended not to comply with the terms of the contract at the inception of the contractual relationship. *See American Trade Partners v. A-1 International Importing,*

755 F. Supp. 1292, 1300 (E.D. Pa. 1990); *Redick v. Kraft, Inc.*, 745 F. Supp. 296, 301 (E.D. Pa. 1990).

Defendants contend they made no misrepresentation upon formation of the contract because they did not form the intent to market Crystal Collectibles until well after the formation of the E&R Co. contract. The earliest evidence of Swarovski's intent to market a smooth line of crystal figurines through Zales was a letter written by Martin Halusa on August 14, 1987 (P-253). The jury could reasonably have believed that Swarovski intended to compete with E&R at the inception of the E&R-Swarovski contract even if it did not decide to do so through Zales until 1987.

Evidence was introduced that Swarovski failed to disclose its intent to compete with E&R Co. in order to induce E&R Co. to test the market for smooth crystal figurines. The Yenawine memorandum of May 31, 1986 to Swarovski suggested that Swarovski would benefit from E&R Co.'s use of the Swarovski name because E&R Co. would facilitate Swarovski's subsequent market entry. The jury could infer from that memorandum and other testimony at trial that Swarovski, intending to use E&R Co. to test the market, failed to disclose that intention to E&R Co. to induce E&R Co.'s expenditure of time and resources to establish the market.

Russo testified that E&R Co. never would have agreed to market Crystal Signatures if it had known the distributorship would not be exclusive. E&R Co. justifiably relied on its understanding that it would have an exclusive right to market Crystal Signatures when it entered into the contract with Swarovski. E&R Co.

expended $850,000 for marketing costs based on its belief that its contract with Swarovski contract [sic] granted it exclusivity. Plaintiff introduced sufficient evidence to support its claim of fraud and the jury verdict in favor of E&R Co. based on fraud should not be set aside.

b. Fraud on E&R, Ltd.

The jury also found that defendants' fraudulent misrepresentations harmed E&R, Ltd. The only post March 31, 1988 fraudulent misrepresentations to E&R, Ltd. alleged by plaintiff were Swarovski statements that it would produce Disney samples. As a result of that misrepresentation, plaintiff prepared to sell Disney figurines at the Disney Expo in the Fall, 1988. When Swarovski failed to produce the samples, plaintiff lost the opportunity to take advantage of its potentially lucrative licensing agreement with Disney.

Assuming that plaintiff justifiably relied on a misrepresentation that Swarovski made knowing it was fraudulent and intending E&R, Ltd. to rely on it, plaintiff failed to prove any harm resulting from the fraudulent misrepresentation. Plaintiff claimed lost profits from Swarovski's failure to produce the Disney figurines. Plaintiff did not claim any damages for its costs spent in reliance on receiving the Disney samples. If plaintiff had not been induced to enter into the Disney license agreement by Swarovski's fraudulent misrepresentation, plaintiff still would not have received any profit from the Disney license agreement.

Plaintiff's ability to profit from the Disney license agreement was dependent on Swarovski producing the samples and, eventually, producing Disney figurines for sale. Plaintiff's lost profits were the result of Swarovski's breach of the E&R-Swarovski agreement by not producing those samples. Swarovski was already contractually required to produce Crystal Signatures figurines for E&R, Ltd. under the exclusive requirements contract. Plaintiff did not lose its opportunity for future profits because of Swarovski's misrepresentation that it would comply with the agreement; E&R, Ltd. lost future profits because Swarovski breached the agreement by failing to produce the Disney samples. The lost profits were awarded by the jury as damages for breach of contract.

Even assuming E&R, Ltd. relied on Swarovski's allegedly fraudulent misrepresentation in deciding to enter into the Disney license agreement, plaintiff did not prove any harm proximately from the fraud itself. Therefore, the jury finding of harm to E&R, Ltd. from defendants fraudulent misrepresentations should be set aside.

4. Trademark Infringement

Liability for trademark infringement redresses a special kind of unfair competition. *See Smithkline Beckman Corp. v. Pennex Products Co.*, 605 F. Supp. 746, 749 (E.D. Pa. 1985). In order to constitute trademark infringement under the Lanham Act, 15 U.S.C. § 1114, defendants' mark must be a "reproduction, counterfeit, copy or colorable imitation" of plaintiff's registered mark, and its use must be likely to cause confusion or mistake, or to deceive the consuming public. Crystal Signatures is E&R,

Ltd.'s registered trademark. The jury found that similarity between defendants' Crystal Collectibles and E&R, Ltd.'s trademark, Crystal Signatures, was likely to cause confusion or mislead consumers into believing that the products came from the same source.

Trademark law divides marks into four categories: (1) arbitrary terms; (2) suggestive terms; (3) descriptive terms; and (4) generic terms. *Dranoff-Perlstein Assocs. v. Sklar*, 1992 U.S. App. LEXIS 14440 (3d Cir. June 17, 1992). A mark is entitled to protection if it is arbitrary, suggestive, or descriptive and possesses secondary meaning. *Id.* Generic terms and descriptive terms that have not acquired secondary meaning are not entitled to protection. *See American Cyanamid Corp. v. Connaught Laboratories, Inc.*, 800 F.2d 306 (2d Cir. 1986).

The only similarity between Crystal Collectibles and Crystal Signatures is the word "crystal." E&R, Ltd. makes no claim to the use of the word "crystal" as crystal is a generic term when used to describe a crystal product and cannot be appropriated for exclusive use by registration of a trademark. *See, e.g., Dranoff-Perlstein* at *28; *American Cyanamid*, 800 F.2d at 308.

In deciding whether a mark is entitled to protection, the overall impression of the entire mark must be considered. "If a common portion of the two conflicting marks is a public domain generic word, the emphasis of the enquiry should be upon the confusing similarity of the nongeneric portion, with the ultimate issue determined by the confusing similarity of the total impression of both marks." *Dranoff-Perlstein* at *28 (citations omitted). The words "collectibles" and "signatures" are not similar and

do not have similar meanings. Plaintiff's registration of the mark Crystal Signatures cannot preclude anyone from using the descriptive term "Crystal Collectibles" to describe collectible crystal figurines. The jury could not reasonably have found that defendants infringed plaintiff's registered mark because the jury's finding of similarity could only have been based on the common use of the word crystal. Liability for violation of trademark will be set aside as incorrect as a matter of law.

5. Unfair Competition

Plaintiff alleged, and the jury found, that defendants engaged in unfair competition in violation of the Lanham Act by infringing on plaintiff's trade dress. To establish a violation of the Lanham Act, 15 U.S.C. § 1125, for trade dress infringement of a product that moves in interstate commerce, plaintiff must prove these three elements: 1) imitation of a non-functional feature, or combination of features, of plaintiff's product, packaging, or design; 2) acquired "secondary meaning" of the imitated feature; and 3) likelihood of consumer confusion of the source of plaintiff's product with that of defendant's product. *American Home Products Corp. v. Barr Laboratories*, 834 F.2d 368, 370 (3d Cir. 1987); *Standard Terry Mills, Inc. v. Shen Mfg. Co.*, 803 F.2d 778, 780 (3d Cir. 1986). The Pennsylvania common law of unfair competition is identical to the provisions of the Lanham Act except that interstate commerce is not required. *Mercury Foam Corp. v. L&N Sales & Mktg.*, 625 F. Supp. 87, 91 n.1 (E.D. Pa. 1985); *Smithkline Beckman Corp.*, 605 F. Supp. at 748 n.1.

The jury found that E&R, Ltd. proved each of the three elements of its unfair competition claim (Appendix C, Unfair Competition Interrogatories 2-4) but the verdict must be set aside because there was insufficient evidence that the Crystal Signatures line had achieved secondary meaning in the marketplace as a matter of law. Therefore, the court need not consider whether plaintiff proved imitation or likelihood of confusion.

A product has achieved secondary meaning when the primary significance of a product feature or term is to identify in the mind of the consumer the source of the product rather than the product itself. *Inwood Laboratories, Inc. v. Ives Laboratories, Inc.*, 456 U.S. 844 (1982). In determining whether E&R, Ltd. met its burden of proving secondary meaning, the court must consider: 1) the length and manner of use; 2) the nature and extent of advertising and promotion; 3) other efforts creating a conscious connection in the public's mind between the appropriated term or feature and the plaintiff's product; 4) the size of the company and its share of the market; and 5) testimony of buyers. *Ginger Group Ltd. v. Beatrice Companies, Inc.*, 678 F. Supp. 555, 560 (E.D. Pa. 1988).

E&R Co. and then E&R, Ltd. had been marketing Crystal Signatures for two years before Crystal Collectibles entered the market; it had spent $850,000 in advertising and promotion of the product. E&R, Ltd. was not the only company distributing crystal figurines but it was the only distributor of crystal figurines manufactured by Swarovski's injection molded technology. Crystal Signatures were displayed in distinctive cases and brochures were available for retailers to distribute to consumers. E&R, Ltd. had used the term "crystal collectibles" in its

advertising to describe the Crystal Signatures product. *See* P-71C.

E&R, Ltd.'s right to use the Swarovski name relates to the breach of contract count; the use of the Swarovski name on a Swarovski product is not a basis for the unfair competition claim. The appearance of the box and the designs copied are the only non-functional features of Crystal Signatures' trade dress that E&R, Ltd. claims Swarovski misappropriated. Plaintiff did not contend that Zales used the same display and lighting. Plaintiff failed to prove that the appearance of the box and the copied designs had achieved secondary meaning.

Proof that E&R made an effort to establish secondary meaning is not sufficient to establish secondary meaning. *See Towle Mfg. Co. v. Godinger Silver Art Co.*, 612 F. Supp. 986, 994 (S.D.N.Y. 1985). There was no evidence that any consumer identified the Crystal Signatures box or the figurines with E&R; although plaintiff was trying to develop a connection in the public's mind with its trade dress, plaintiff is not entitled to protection for "secondary meaning in the making." *See Laureyssens v. Idea Group Inc.*, 1992 U.S. App. LEXIS 10643 (2d Cir. May 15, 1992). The doctrine of secondary meaning ensures that something worth protecting exists before it limits the freedom of a competitor to compete by copying. *Id.* Plaintiff failed to introduce any evidence that consumers had begun to recognize the Crystal Signatures' trade dress; the jury finding for plaintiff on the unfair competition claim is not supported by the evidence.

Plaintiff's trademark and unfair competition claims are in reality a reassertion of the claim that Swarovski

breached the contract by marketing a competing line of injection molded crystal figurines. The jury's verdict and punitive damage award for trademark infringement and unfair competition must be set aside as incorrect as a matter of law. *See* Appendix C, Trademark & Unfair Competition.

6. Trade Secret

The burden of proof is on the plaintiff to show both a trade secret and misappropriation by defendants. *Gilbert v. Otterson*, 550 A.2d 550, 555 (Pa. Super. 1988), *app. denied*, 562 A.2d 320 (Pa. 1989). Pennsylvania courts have adopted the definition of a trade secret given in the Restatement of Torts § 757 comment b (1939):

> A trade secret may consist of any formula, pattern, device or compilation of information which is used in one's business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it. It may be a formula for a chemical compound, a process of manufacturing, treating or preserving material, a pattern for a machine or other device, or a list of customers.

SI Handling Systems v. Heisley, 753 F.2d 1244, 1255 (3d Cir. 1985).

E&R Co. made a presentation to Swarovski at which time it disclosed its marketing strategy for Crystal Signatures. Plaintiff contended that the presentation was to demonstrate E&R Co.'s ability to distribute the injection molded figurine line successfully and Swarovski was not

entitled to use that information in competing with plaintiff.

Swarovski's internal documents established that Swarovski gained an advantage from E&R Co.'s disclosure of its marketing strategy. The jury could reasonably have found that Swarovski misappropriated E&R Co.'s marketing strategy and used it to its own advantage in marketing Crystal Collectibles.

Defendants claim that plaintiff cannot now assert that Swarovski misappropriated its marketing strategy because that position is inconsistent with plaintiff's claim on damages. Plaintiff claimed that marketing of Zales Crystal Collectibles was inferior to the marketing of Crystal Signatures so that Crystal Collectibles' sales were not an accurate measure of the lost future profits of Crystal Signatures. These positions are not inconsistent; Swarovski may have attempted the use of E&R Co.'s marketing strategy without being as successful as plaintiff would have been. The finding of liability in favor of plaintiff on trade secret will not be set aside. However, plaintiff failed to meet its burden of proof on damages for trade secret misappropriation and the punitive damages awarded on that claim were duplicative, so they will be set aside. *See infra* III.B.3.

B. DAMAGES – Motion to Alter or Amend the Verdict or Grant a New Trial

Defendants move the court to alter or amend the verdict on damages or grant a new trial on damages. A trial judge can grant a new trial or alter or amend a

verdict under Federal Rule of Civil Procedure 59. Rule 59 provides:

> (a) Grounds. A new trial may be granted to all or any of the parties and on all or part of the issues (1) in an action in which there has been a trial by jury, for any of the reasons for which new trials have heretofore been granted in actions at law in the courts of the United States. . . .
>
> * * *
>
> (e) Motion to Alter or Amend a Judgment. A motion to alter or amend the judgment shall be served not later than 10 days after entry of the judgment.

A trial court has broad discretion in ruling on a motion for a new trial under Rule 59(a) on the grounds of improperly admitted or excluded evidence, misconduct of counsel, an improper charge to the jury, or newly discovered evidence. *See Lind v. Schenley Indus., Inc.*, 278 F.2d 79, 90 (3d Cir.), *cert. denied*, 364 U.S. 835 (1960). A trial judge's discretion is more limited in granting a new trial because the jury's verdict is against the weight of the evidence. *See id.* at 90.

Rule 59(e) was enacted to allow a district court to rectify its own mistakes. *See White v. New Hampshire Dept. of Employment Secur.*, 455 U.S. 445, 451 (1982) (citing the Advisory Committee Report to Rule 59). A Rule 59(e) motion can be granted if there is a change in the controlling law, new evidence not previously available becomes available, or a need to correct a clear error of law or prevent manifest injustice. *See Atkins v. Marathon LeTourneau Co.*, 130 F.R.D. 625 (S.D. Miss. 1990); *Natural*

Resources Defense Council, Inc. v. U.S. E.P.A., 705 F. Supp. 698 (D.D.C. 1989).

A court may not grant a motion to alter or amend the verdict under Rule 59(e) if it would defeat a party's right to a jury trial on the issue. *See* Wright & Miller, *supra* at § 2817. A judge may not set aside a verdict merely because the judge might have awarded a different amount of damages. *See Toombs v. Manning*, 640 F. Supp. 938, 940 (E.D. Pa. 1986), *aff'd in part and rev'd in part*, 835 F.2d 453 (3d Cir. 1987); 11 Charles A. Wright & Arthur R. Miller, *Federal Practice and Procedure* § 2807 (1991).

Defendants seek to set aside the damages verdicts for lost profits, reputation damages, trade secret, and punitive damages.

1. Lost Profits

The compensatory damage award of lost profits in the amount of $25,000,000 was neither against the weight of the evidence nor manifestly unjust.

a. Limitation of Damages: Statute of Frauds

Defendants concede the existence of a contract with E&R Co. but contend that Swarovski liability for breach of the E&R contract is limited by the Statute of Frauds to the amount of goods admitted or stated in written memoranda signed by Swarovski, *ie.*, the amount set forth in the purchase orders submitted to Swarovski by E&R Co.

A contract for the sale of goods for the price of $500 or more must be memorialized by a writing signed by the

party against whom enforcement is sought. 13 Pa. C.S.A. § 2201(a). The contract is not enforceable under § 2201(a) "beyond the quantity of goods shown in such writing." *Id.* However, § 2306 of the Pennsylvania Commercial Code allows quantity to be measure by the seller's output or the buyers requirements. The Third Circuit interprets § 2306 as allowing open quantity agreements when the parties' clear intention is to enter into more than a simple buy and sell agreement. *See Advent Systems Ltd. v. Unisys Corp.*, 925 F.2d 670 (3d Cir. 1991). Plaintiff characterizes the agreement as a requirements contract for the life of the product.

The jury reasonably found that the E&R-Swarovski contract was for the entire "product line" for the life of the product. Russo testified at trial that Crystal Signatures was a line of collectibles; collections of figurines with common themes were to be marketed together although additional items would be added to each group from time to time. A telex from Swarovski, Pl. Ex. 12, stated that Swarovski was prepared to begin production on the series listed and gave exclusivity to E&R Co.; this also supported plaintiff's claim that the E&R-Swarovski agreement was for the entire product line.

The jury could have reasonably inferred from the evidence that the contract between Ebeling & Reuss and Swarovski was an exclusive requirements contract. The defendants tried to persuade the jury that the contract was limited to the quantities set forth in the purchase orders. The jury chose not to ignore evidence that the agreement covered plaintiff's requirements for the entire product line and not just the figurines that had been ordered. Even if no specific amount was stated, such a

contract satisfies the quantity requirements of the Statute of Frauds under § 2306.

b. Speculativeness

Under Pennsylvania law, lost profits may be recovered in a contract action if (1) established with reasonable certainty; (2) the proximate consequence of the wrong; and (3) reasonably foreseeable. *Delahanty v. First Pennsylvania Bank, N.A.*, 464 A.2d 1243, 1258 (Pa. Super. 1983). Proof of damages need not be mathematically precise, but the evidence must establish damages "with a fair degree of probability." *Exton Drive-In, Inc. v. Home Indemnity Co.*, 261 A.2d 319, 324 (Pa. 1969), *cert. denied*, 400 U.S. 819 (1970).

The Pennsylvania Supreme Court has been skeptical of claims for lost profits by a "new and untried business." *Exton* 261 A.2d at 324. *See also Delahanty*, 464 A.2d at 1260; *Pollock v. Morelli*, 369 A.2d 458, 463 (Pa. Super. 1976). However, an award may be made "where such a loss was reasonably foreseeable to the parties at the time that the contract was entered and where those damages are capable of proof of reasonable certainty." *General Dynafab, Inc. v. Chelsea Industries, Inc.*, 447 A.2d 958, 960 (Pa. Super. 1982).

In *General Dynafab*, plaintiff, arguably a newcomer to the business, was able to show commitments of orders from four sources; "there was significant interest in [its] product before the contract breach occurred," so that evidence of lost profits should have been submitted to the

jury. *Id.* The *Delahanty* court stated the practice in Pennsylvania is to "liberally allow evidence of alleged profits to be submitted to the jury." 464 A.2d at 1260. The court must then analyze the evidence and the circumstances and make its own determination whether as a matter of law the damages are too speculative.

Ebeling & Reuss had a 100 year history of distributing goods for various manufacturers to retail outlets in the United States. Ebeling & Reuss had not distributed Swarovski molded crystal objects, but Ebeling & Reuss had been distributing this type of product successfully for many years; Swarovski had chosen E&R Co. as its distributor so it believed E&R Co. had the resources and capability to succeed in such an endeavor. E&R, Ltd. continued the business in much the same way as E&R Co.; E&R, Ltd. continued using the name Ebeling & Reuss Co., and distributed the same type of products to the same customers.

Ebeling & Reuss had a reputation in the marketplace for distributing successful products. There was evidence that Ebeling & Reuss had been successful in its introduction of the product. Ebeling & Reuss's profits depended on its ability to sell the crystal figurines manufactured by Swarovski to United States retailers. Ebeling & Reuss, Ltd.'s proof of this rested on the testimony of Russo, the company president, and Cook, its expert witness. Both relied heavily on the initial projections Russo formulated when E&R Co. decided to distribute the Crystal Signatures line. The Russo projections were not unreliable just because the actual sales of Crystal Signatures were not as great as predicted; the jury believed, based on sufficient evidence, that the loss of sales of Crystal Signature items

was caused by the defendants. Defendants cannot use their own actions to defeat plaintiff's claim.

This case is distinguishable from *Advent Systems Ltd. v. Unisys Corp.*, 925 F.2d 670 (3d Cir. 1991), where plaintiff's expert relied on industry projections much higher than actual industry sales data. Unisys had agreed to distribute an electronic document management system developed by Advent. Unisys breached the distribution agreement, and marketed its own electronic document management system instead. In its suit against Unisys, an expert for Advent testified to the projected lost profits suffered by Advent as a result of the breach. The projections were based on a market analysis prepared at the time electronic document management systems were introduced into the market and predicted industry-wide sales. At trial, Unisys introduced actual industry results showing that the projections relied on by plaintiff's expert were overly optimistic. The Court of Appeals remanded the case on other grounds after commenting that the court had serious doubts whether the record was adequate to support the lost profits verdict.

Mr. Cook also relied on projections of sales made prior to introduction of the product, but they applied only to Crystal Signatures' projected sales and not industry-wide sales of crystal collectible miniature figurines. Defendants did not offer actual industry sales figures to show that sales in the crystal or figurine markets were down in general during the period the harm to Ebeling & Reuss occurred.

Defendants offered the poor sales of the Zales Crystal Collectibles line to show that the projections on which

Russo and Cook relied were flawed. Defendants did not establish that the marketing of Zales Crystal Collectibles was comparable to the marketing of Crystal Signatures. Defendants failed to introduce any evidence that the poor performance of Zales Crystal Collectibles was representative of performance in the industry. Plaintiff introduced evidence the jury reasonably believed – namely, that the Swarovski promotion and marketing of the Crystal Collectibles line was inferior to the professional approach Ebeling & Reuss would have used in marketing the Crystal Signatures line.

The jury could have reasonably concluded that the marketing of the Crystal Signatures line was not a new business for E&R Co. Russo's projections were based on his many years in the business and were sufficiently reliable. The verdict awarding plaintiff $25,000,000 for lost profits was not excessive since the jury found E&R's distributorship was to have been exclusive for the life of the product.

2. Reputation Damages

Damage for harm to reputation proximately caused by tortious interference with contractual relations is recoverable in Pennsylvania. *See Tose v. First Pennsylvania Bank,* 648 F.2d 879, 898 (3d Cir. 1981). Plaintiff alleged SAL tortiously interfered with plaintiff's prospective contractual relations with retailers by sending the Metcalfe letter. Plaintiff claimed the Metcalfe letter harmed its reputation in the collectibles industry by casting doubt on the authenticity of collectibles distributed by Ebeling & Reuss.

Plaintiff failed to prove actionable tortious interference and judgment notwithstanding the verdict will be entered for defendants on the tortious interference count. *See supra* III.A.2. Therefore, there is no liability finding to support damages for harm to reputation.

3. Trade Secret Damages

Defendants contend that the trade secret damages verdict of $291,364 should be set aside because it is unsupported by the evidence. Plaintiff introduced evidence at trial that Swarovski used the marketing strategy Swarovski had learned from confidential communications with E&R Co. when it marketed Zales Crystal Collectibles. Plaintiff, in its closing argument on trademark, unfair competition, and trade secret, asked the jury to award $291,364 in damages to deprive Swarovski of profits earned by misappropriation of plaintiff's trade secret.

Plaintiff's demand for an award of Swarovski profits in that amount required a succession of inferences. (N.T. 6/21/90 at 47-48) Plaintiff asked the jury to infer that Swarovski charged Zales roughly the same as it charged Ebeling & Reuss. Plaintiff estimated the unit cost of Crystal Collectibles based on a "mid-point" retail price for Crystal Collectibles. The figures on which plaintiff relied other than the number of pieces sold were no more than uninformed estimates. There was evidence of the number of Zales Crystal Collectibles pieces sold but no reliable evidence of the profit from their sale. The verdict of $291,364 was entirely speculative and will be set aside. (Appendix C, Damages Interrogatory 7a.)

4. Punitive Damages

a. Constitutionality

The jury awarded punitive damages for defendants' tortious conduct of tortious interference, fraud, trademark infringement, unfair competition, and misappropriation of a trade secret. Defendants argue that the punitive damages awarded under Pennsylvania law must be set aside because the award violated the Fourteenth Amendment's due process clause. Defendants concede that the jury charge on punitive damages "was based on an accurate understanding of Pennsylvania law today." Defendants' Memorandum of Law at 21. Nevertheless, defendants assert that Pennsylvania law violates the due process clause of the Fourteenth Amendment because the amount of the award is in the sole unguided discretion of the jury.

In *Pacific Mutual Life Insurance Co. v. Haslip*, 111 S. Ct. 1032, 113 L. Ed. 2d 1 (1991), the Supreme Court, denying a similar challenge to Alabama law, held that common law assessment of punitive damages does not deny due process and is not *per se* unconstitutional. Plaintiffs had sued an insurance agent and Pacific Mutual Insurance Company for fraudulently misappropriating insurance premiums paid for plaintiffs' coverage through another insurance company. The jury returned a plaintiff's verdict including punitive damages in the amount of $840,000. In determining the constitutionality of punitive damages, the Court considered reasonableness and adequate guidance from the trial court. *Id.* The Court found that discretion to award punitive damages was exercised within reasonable constraints where the jury had been instructed

that the purpose of punitive damages was confined to deterrence and retribution.

Pennsylvania law also allows punitive damages for punishment and deterrence. *See Kirkbride v. Lisbon Contractors, Inc.*, 555 A.2d 800, 803 (Pa. 1989). A Pennsylvania jury's decision to award punitive damages is not without guidance; it must consider the factors set forth in § 908(2) of the Restatement (Second) of Torts. *See Feld v. Merriam*, 485 A.2d 742 (Pa. 1984).

Section 908(2) permits punitive damages to "be awarded for conduct which is outrageous, because of the defendant's evil motive or his reckless indifference to the rights of others. Punitive damages must be based on conduct which is 'malicious,' 'wanton,' 'reckless,' 'willful,' or 'oppressive.' " *Feld* at 747-48 (citations omitted). Section 908(2) states, "[i]n assessing punitive damages, the trier of fact can properly consider the character of the defendant's act, the nature and extent of the harm to the plaintiff that the defendant caused or intended to cause and the wealth of the defendant." As Pennsylvania law provides jurors with at least the same guidance as the common law of Alabama, the punitive damage award is not *per se* unconstitutional.

In *Pacific Mutual*, the Supreme Court also considered whether Alabama's post-jury-verdict standard of review satisfied the due process requirements of the Fourteenth Amendment. The Court found that Alabama's standard of review met federal constitutional requirements where: the state's post verdict test insures meaningful and adequate review by the trial court whenever a jury has awarded punitive damages; the state's highest court

applies appellate review standards that impose a meaningful and sufficiently definite constraint on the discretion of state fact finders in awarding punitive damages; and such standards have a real effect resulting in reduction of punitive damages awards in post verdict review by the trial judges and state supreme court.

Defendants assert that Pennsylvania law impermissibly restricts the exercise of judicial discretion to set aside excessive damage awards. Defendants argue that "a court should be able to set aside an award on the grounds that it is unfair, not reasonably related to the actual harm or unwarranted by the evidence." Defendants' Memorandum of Law at 22. The Pennsylvania test, as set forth in *Kirkbride,* not only imposes sufficiently definite and meaningful constraint on the discretion of the fact finder but insures meaningful and adequate review.

Pennsylvania affords review of the punitive damage award both at the trial and appellate level. *See, Sulecki v. Southeast National Bank,* 516 A.2d 1217, 1220 (Pa. Super. 1986). Under Pennsylvania law, a court may set aside a punitive damage verdict "in those rare instances" where "the amount of punitive damages may be so disproportionate when compared to the character of the act, the nature and extent of the harm and the wealth of the defendant, that it will shock the court's sense of justice." *Kirkbride,* 555 A.2d at 803. Pennsylvania law somewhat restricts a court's ability to set aside a verdict, but Pennsylvania courts have not found this burden insurmountable. The Pennsylvania standard has real effect when applied by Pennsylvania courts to jury awards. *See, e.g., Southeast National Bank v. Sulecki,* 516 A.2d at 1217 (Superior court affirms trial court's decision to reduce punitive

damage award). Post verdict review by Pennsylvania appellate courts has also resulted in the reduction of punitive awards. *See, e.g., Feld v. Merriam,* 485 A.2d 742 (Pa. 1984) (Pennsylvania Supreme Court granted new trial where issue of punitive damages improperly went before jury); *Smith v. Celotex Corp.,* 564 A.2d 209 (Pa. Super. 1989) (Pennsylvania Superior Court granted judgment NOV to appellant as to punitive damages).

Pennsylvania law makes clear that punitive damages awards do not have to be related to the compensatory damages suffered. In adopting §902 of the Restatement (Second) of Torts, Pennsylvania law makes the comparison not the relationship of the punitive damages to the compensatory damages but the relationship of the punitive damages to the wealth of the tortfeasor in order "to deter him or others from similar conduct." *See Kirkbride,* 555 A.2d at 803. In light of these policies, guidelines and constraints under Pennsylvania law and their similarity to those in Alabama explicitly approved by the Supreme Court in *Pacific Mutual,* an award of punitive damages under Pennsylvania law satisfies the due process requirement of the Fourteenth Amendment.

The court will now exercise such a review of the jury verdict on punitive damages.

b. Excessiveness of Punitive Damages Verdict

Defendants contend that the punitive damage awards are duplicative and excessive. The claims for breach of contract, promissory estoppel, tortious interference,

fraud, and civil conspiracy were sent to the jury first. The jury awarded a total of $33,850,000 in compensatory damages and $16.5 million in punitive damages on those claims. *See* Appendix B. The jury next heard closing argument and charge of the court on the trademark, unfair competition, and trade secret claims; no additional evidence was presented. The jury returned an additional punitive damage award of $2.5 million on the trademark and unfair competition claims and an additional award of $291,364 in compensatory damages and $2.5 million in punitive damages on the trade secret claim. *See* Appendix C.

Pennsylvania follows section 908(2) of the Restatement (Second) of Torts in considering the following three factors in awarding punitive damages: (1) the character of the act; (2) the nature and extent of the harm; and (3) the wealth of the defendant. *Kirkbride*, 555 A.2d at 803. A court may set aside a jury award of punitive damages in those rare instances when the punitive damages are so disproportionate to those factors that it shocks the court's sense of justice. *Id.*

Swarovski's net worth was stipulated to be in excess of $200 million; compensatory damages on all claims totalled $34,141,364 and punitive damages on all claims totalled $21,500,000. As a result of the judgment n.o.v. on liability, total compensatory damages are reduced to $25,850,000. The $2.5 million punitive damage award on the trademark and unfair competition claims was set aside because liability was not established. *See supra* III.A.4&5. Because of the likelihood the $2.5 million punitive damage award for misappropriation of a trade secret was duplicative, the court will set aside that award also.

Therefore, the total award of punitive damages is $16.5 million.

The punitive damages are not disproportionate to the nature of defendants' actions. Defendants were using their capacity to make injection molded figurines to compete with E&R, Ltd. while refusing to deliver the Disney figurines in breach of contract. The jury also saw and obviously reacted to the arrogance of defendants' witnesses. The jury clearly found defendants' conduct outrageous as it found against defendants on all counts.

The punitive damages are not disproportionate to the nature and extent of the harm. The resulting total award of $16,500,000 in punitive damages is less than the total award of $25,850,000 in compensatory damages. Plaintiff's business was in effect destroyed by defendants' conduct; plaintiff ultimately filed for bankruptcy protection. The award of punitive damages is not excessive even though the court will set aside the jury findings on liability for tortious interference and fraud against E&R, Ltd. The jury determined the amount of punitive damages based on the nature of defendants' actions, not the theory of defendants' liability.

The defendants' net worth was stipulated to be in excess of $200 million dollars. The punitive damage award of $16.5 million is less than 10% of that amount. Considering the conduct of defendants, the harm to plaintiff that defendants intended to cause to avoid the contract, and the extreme wealth of defendants (far in excess of the amount stipulated), this court is not persuaded to reduce the punitive damage award further.

C. MOTION FOR NEW TRIAL

Federal Rule of Civil Procedure 59(a) allows a court to grant a motion for new trial when there has been a trial by jury "for any of the reasons for which new trials have heretofore been granted in actions at law in the courts of the United States." Fed. R. Civ. P. 59(a). Defendants complain of numerous errors in the three week trial of this action.

1. Expert Testimony

a. Plaintiff's expert properly qualified

Plaintiff offered Stephen B. Cook as an expert in valuing a product line. Mr. Cook testified on voir dire that he had valued product lines in his work with Price Waterhouse, he had been to conventions in the retail merchandising field, and he had worked in the collectibles industry for E&R in high school and college. (N.T. 6/7/90 at 66-73) Defense counsel challenged Mr. Cook's expertise in valuing a product line because of Mr. Cook's admitted lack of expertise in evaluating the aesthetics of products. Defendants claim that knowledge of the general public's interest in a new product that had never before been marketed was necessary for valuing that new product.

A witness may testify as an expert if he has such skill, knowledge, or experience in the field as to make it appear that his opinion will probably aid the trier of fact. *Hines v. Conrail,* 926 F.2d 262, 272 (3d Cir. 1991); *Aloe Coal Co. v. Clark Equipment Co.,* 816 F.2d 110, 114 (3d Cir.), *cert. denied,* 484 U.S. 853 (1987). A proffered expert witness

must possess knowledge or skill in the area of his testimony greater than that of the average layman. *Aloe Coal Co.*, 816 F.2d at 114. The standard for qualification as an expert under Federal Rule of Evidence 702 is liberal. *Hines*, 926 F.2d at 272. Credibility determinations are for the jury. *In re Paoli R.R. Yard PCB Litigation*, 916 F.2d 829, 858 (3d Cir. 1990).

Mr. Cook's testimony on the value of the Crystal Signatures product line was helpful to the jury. Mr. Cook's experience in valuing product lines, his training in retail merchandising, and his experience working for E&R gave him greater knowledge in valuing a new crystal collectible product than the average layman regardless of the jury's ability to decide for itself whether the product line was aesthetically pleasing that it would be well received in the market. Mr. Cook used the initial response of retailers to the product line and the opinions of others in the giftware industry to determine the value of the Crystal Signatures product line; this was a rational basis for an expert opinion. The court's finding that Mr. Cook was qualified to testify as an expert on valuing the product line at issue was not erroneous.

b. Mr. Cook's testimony

The court allowed Mr. Cook to testify to statements made by other people in the giftware industry about Mr. Russo's reputation in the industry and Mr. Russo's accuracy in making projections. Defendants claim this was inadmissible hearsay. Defendants concede that an expert can testify to hearsay statements if the expert relied on those statements in reaching his opinion and they are the

type of statements upon which experts in the field customarily rely. *See In re Japanese Electronic Products Antitrust Litigation*, 723 F.2d 238, 277 (3d Cir. 1983), *rev'd on other grounds*, 475 U.S. 574 (1986).

Mr. Cook testified that Price Waterhouse has a policy requiring a background check on a person before the company will prepare prospective financial information for that person. Mr. Cook stated that the purpose of this background check is to verify the reliability of assertions made by the person or entity for whom the financial projections are prepared. Before Mr. Cook would rely on a client's assertions in doing his valuation work, he had to have confidence in the reliability of the person making them.

In preparing the Crystal Signatures projections, Mr. Cook relied in part on projections prepared by Mr. Russo. Therefore, Mr. Cook had to check Mr. Russo's reputation for accuracy in the giftware industry. Mr. Cook's statement that he did not rely on the background check of Mr. Russo in formulating his opinion must be taken in the context of what he had already said. The opinion to which he was referring at that time was the final damages projection. Mr. Cook earlier had testified that he did rely on the background check of Mr. Russo in formulating his opinion that Mr. Russo's sales projections were reliable. He then used those sales projections in formulating his ultimate opinion on damages. Mr. Cook reasonably relied on the statements of people in the giftware industry in formulating his opinion in accordance with the standard and accepted practice in his field; therefore, it was permissible for him to testify about those statements.

c. Defendants' expert witness

Defendants complain that the testimony of their expert witness, Margaret McKinley, was unfairly limited to the testimony she gave in her depositions. At trial, plaintiff argued that Ms. McKinley should not be permitted to criticize Mr. Cook's testimony or the method of reaching his result except to the extent she had been critical in her depositions. The court reviewed Ms. McKinley's deposition testimony and then informed counsel and Ms. McKinley of those opinions to which Ms. McKinley was limited based on her deposition testimony. Defendants argue that such a limitation was improper.

At the final pretrial conference on May 21, 1991, the court informed counsel that experts might not testify to anything not provided to the opposing party in advance either by answers to interrogatories, by deposition, or by expert report. The court specifically stated that Mr. Russo, plaintiff's witness, would not be allowed to express any opinions he had not already expressed. The court then stated that the information in Ms. McKinley's report would be the extent of her testimony.

Although the court made its order perfectly clear prior to trial, defendants attempted to have their expert testify to previously undisclosed opinions about the reliability of Mr. Cook's projections. When plaintiff objected, the court reviewed the depositions of Ms. McKinley. The court found that plaintiff had repeatedly asked Ms. McKinley the basis for disagreement with the projections. Therefore, the court limited Ms. McKinley's testimony to those opinions of which plaintiff had notice.

Defendants argue that a defense expert cannot be limited to opinions given prior to trial because the expert does [sic] not yet heard plaintiff's expert's testimony. That is not a valid argument because plaintiff's expert was also limited to those opinions of which he gave defendants notice prior to trial. Therefore, each side had notice and an opportunity to respond to the testimony of the other's experts. This procedure, consistent with Local Rule 21, assures that neither side is unfairly surprised by the expert testimony at trial.

Defendants contend that they know of no principle that allows limitation of a defense expert's criticism of plaintiff's expert's testimony by reference to the defense expert's pretrial deposition. The Federal Rules of Civil Procedure apply to defendants as well as plaintiffs. Rule 37(b)(2)(B) gives the court the power to prohibit a party who fails to comply with an order for discovery under Rule 26(f) from introducing designated matters into evidence. The Court of Appeals has upheld an order preventing a plaintiff from using any expert testimony at all because of the plaintiff's failure to give notice of the basis for the expert's opinion despite repeated requests from the defendants. *See Hagans v. Henry Weber Aircraft Distrib., Inc.*, 852 F.2d 60 (3d Cir. 1988). In another case, the Court of Appeals upheld a district court's exclusion of a witness' testimony where counsel represented at a pretrial conference that the witness would only be relying on specific data but, at trial, it became apparent that the witness has relied on additional data. *See United States v. 68.94 Acres of Land in Kent County*, 918 F.2d 389, 396-97 (3d Cir. 1990).

This court informed counsel that expert witnesses would not be permitted to testify to undisclosed opinions. The court's limitation on Ms. McKinley's testimony was an appropriate sanction under Rule 37 for defendants' failure to disclose all the bases for its expert's opinions. Defendants having failed to disclose fully the opinions of their expert, have no grounds for new trial because the testimony of their expert was limited at trial at the request of plaintiff.

Defendants further claim that Ms. McKinley was admonished to answer only "yes" or "no" to clearly misleading questions. The court instructed Ms. McKinley to answer "yes or no or I can't answer" if the question was susceptible of such an answer. (N.T. 6/12/90 at 36) The court told the witness that defendants' attorney would have the opportunity to bring out anything else on redirect. The court's instruction was clearly proper. The court had similarly restricted Mr. Russo's testimony on cross-examination; Mr. Russo asked if he could explain an answer and the court informed him he would have to wait for redirect. (N.T. 6/7/90 at 12)

Defendants contend that the court favored plaintiff by allowing plaintiff's witnesses great freedom in their testimony and restricting defendants' cross-examination. Defendants have not pointed to any testimony of plaintiff's expert of which defendants were not given notice prior to trial. Defendants admit they chose not to object to any of Mr. Cook's testimony. The record of this extended trial clearly reveals that both sides were treated fairly by the judge; the record clearly shows it was the jury, not the judge, that favored the plaintiff based on the evidence at trial.

2. Prejudicial Trial Errors

Defendants claim they are entitled to a new trial because of prejudicial trial errors relating to whether defendants' conduct caused Crystal Signatures' failure in the marketplace. They contend hearsay testimony about the Metcalfe letter was improperly admitted, defendants' cross-examination of Mr. Russo was unfairly restricted, and plaintiff's counsel knowingly elicited false testimony about late deliveries.

a. Hearsay testimony

Mr. Russo testified that the Metcalfe letter (implying that E&R Co. was not authorized to use the Swarovski name) had a devastating effect on the marketing of Crystal Signatures as well as the reputation of Ebeling & Reuss. He claimed retailers would not buy Crystal Signatures because they thought the product line was not authentic, that is, not made by Swarovski; authenticity is very important in the collectibles industry. Over defendants' objection, the court allowed Mr. Russo to testify to what his salespeople reported to him about their experiences trying to sell Crystal Signatures after the Metcalfe letter and what the salespeople told him the retailers had said.

Defendants complain in particular that Mr. Russo testified that "unidentified retailers were saying to the unidentified salesmen [] that 'this merchandise is counterfeit, it's not authentic and, therefore, we will not buy it.' " (Def. Brief at 36) Defendants mischaracterize Mr. Russo's testimony. Mr. Russo testified that his salesmen

"had to deal with so many negatives trying to sell the line that they became afraid of it." (N.T. 6/5/90 at 99) When the court asked Mr. Russo to clarify what he meant when he said "it," Mr. Russo testified as follows:

> It refers to the attitude in the marketplace that said this merchandise is counterfeit, it's not authentic and, therefore, we will not buy it. And, so they couldn't sell it. (N.T. 6/5/90 at 100)

Defendants moved to strike this answer and the court denied the motion.

Defendants classify this statement as classic hearsay. The Federal Rules of Evidence define hearsay as "a statement, other than one made by the declarant while testifying at the trial or hearing, offered in evidence to prove the truth of the matter asserted." Fed. R. Evid. 801(c). Mr. Russo's testimony was intended to prove that Ebeling & Reuss's reputation in the marketplace was harmed by the Metcalfe letter and that retailers would not buy Crystal Signatures. Clearly, Mr. Russo's testimony was not intended to prove that the merchandise was in fact counterfeit or not authentic. At most, only the phrase "we will not buy it" was offered for the truth of the matter asserted in Mr. Russo's explanation of why salespeople were not selling his product line.

Mr. Russo did not claim that a particular retailer said "we will not buy it." He testified that the attitude in the marketplace was that retailers would not buy Crystal Signatures because its authenticity had been questioned. Therefore, "we will not buy it" is not a statement, *i.e.*, an assertion or nonverbal conduct intended by the person as

an assertion, because there was no declarant. *See* Fed. R. Evid. 801(a)&(b).

Even if the court had admitted the complained of testimony in error, any such error was harmless. Mr. Russo testified that, as a result of the Metcalfe letter, he personally had to spend much time traveling around the country discussing the authenticity of the line and Ebeling & Reuss' permission to use the name. He further stated that Helmut Swarovski had admitted the Metcalfe letter was very damaging to Crystal Signatures. Martin Halusa also agreed the letter never should have been sent. The transcript contains ten pages of Mr. Russo's testimony about the effect of the Metcalfe letter. (N.T. 6/5/90 at 96-106) There was clearly sufficient credible evidence of the effect of the Metcalfe letter without the testimony to which defendants objected.

b. Defendants' Cross-Examination Restricted

Defendants argue that the court unfairly restricted cross-examination of Mr. Russo and Mr. Cook. During cross-examination of Mr. Russo, defendants wanted to display to the jury several exhibits not yet admitted into evidence. The court informed defense counsel that he could display exhibits already admitted and part of any exhibit not yet admitted if he were using that part during his cross-examination.

During his cross-examination of Mr. Russo, defense counsel attempted to display to the jury documents not yet in evidence. The court again explained to defense counsel that defendants could call Mr. Russo during their

own case, but they could not introduce exhibits not in evidence during plaintiff's case. (N.T. 6/7/90 at 6-9) When defense counsel again tried to display an exhibit not yet in evidence, the court once again informed him he could not display it to the jury. Defense counsel responded that he would not proceed with his cross-examination, but would examine Mr. Russo during the defendants' case instead. Defense counsel then stated that he found the court's instructions on how he could conduct the cross-examination so limiting as to be prejudicial. (N.T. 6/7/90 at 25)

It is well-established in the federal courts and a majority of states that cross-examination is properly limited to matters raised on direct examination and impeachment. *See McCormick on Evidence* § 21 (2d Ed. 1979). The court, in its discretion, may prohibit a party from introducing evidence during the presentation of its opponent's case. The court properly prohibited defendants from going beyond the scope of Mr. Russo's direct testimony during cross-examination. The court informed defense counsel that he could not introduce all documents that might be admissions of plaintiff during his cross-examination of plaintiff's witness. Defense counsel could ask questions about any part of a document that pertained to the cross-examination of Mr. Russo but introduce the entire document in defendants' case. (N.T. 6/7/90 at 7) Defense counsel made a strategic decision to wait to question Mr. Russo until defendants' case.

Defense counsel also claims he was improperly restricted in his examination of Mr. Cook. Defendants refer to a remark made by the court during cross-examination of Mr. Cook during plaintiff's rebuttal. Defense

counsel wished to question Mr. Cook about weekly order reports that were not in evidence. The court stated that defense counsel had no reason to believe the reports would become part of the record. (N.T. 6/14/90 at 74) At this point, defendants had already rested without offering the reports as exhibits. Defendants were not prejudiced by the court's statement that counsel had no reason to believe the reports would be admitted.

c. False Testimony

Defendants contend the court committed prejudicial error in ruling that cross-examination was an adequate curative if plaintiff's counsel had knowingly elicited false testimony. During direct examination of Mr. Russo, the court admitted plaintiff's exhibit 156, listing deliveries of Crystal Signatures. (N.T. 6/5/90 at 63) Mr. Russo testified that this list of shipments was E&R Co.'s inventory as of December 31, 1986.

Defendants objected to Mr. Russo's allegedly false testimony about this document. Defense counsel claimed the document was incomplete because it related to only three of the six series of Crystal Signatures product. Defendants argued that testimony the shipments listed on P-156 represented the entire Crystal Signatures inventory must be false since the document related to only a portion of the collection.

The court informed defense counsel that he could cross-examine with regard to P-156 and point out any inconsistencies then. On cross-examination, defense

counsel showed Mr. Russo two additional reports in German. Defendants asserted that these two pages were part of the document introduced as P-156. Mr. Russo could not testify about these pages because he was unable to read German. Defendants did not have these pages translated and, even in their motion for new trial, cannot establish that P-156 was in fact incomplete or that Mr. Russo's testimony was false.

The court is not prepared to order a new trial based on defense counsel's speculation that Mr. Russo's testimony was false. The court is shocked that defense counsel would accuse plaintiff's counsel of intentionally eliciting false testimony without proof.

3. Verdict Against Weight of Evidence

Defendants claim the jury's verdict was against the evidence and the weight of the evidence. Defendants' motion for a new trial essentially takes each jury finding and argues that no credible evidence was introduced to support a finding for plaintiff.

Defendants ask the court to discount Mr. Russo's testimony because they claim Mr. Russo defrauded defendants, Alco Standard, and the institution financing the E&R, Ltd. purchase of E&R Co. from Alco Standard. Defendants allege Russo delayed delivery of merchandise to E&R Co. so E&R, Ltd. did not have to pay as much to buy it from Alco Standard. Mr. Russo testified that he delayed the orders for other reasons and that additional

bank financing was available had E&R Co. acquired additional merchandise in inventory because the bank financing was asset-based lending. In asset-based lending, the amount of a bank loan is proportional to the value of the assets. Mr. Russo's explanation of the delay was credited by the jury. The court is not willing to discount his testimony.

Defendants claim that E&R, Ltd. could not have financed purchase of the quantities required under the contract and therefore could not have made the profits plaintiff claimed. Plaintiff introduced testimony from its banker, Mr. Richard Slimmer of Bucks County Bank, who stated that the bank was ready and willing to loan E&R, Ltd. sufficient funds. Mr. Slimmer's testimony was credible.

Defendants discount Mr. Russo's testimony for lack of credibility and then argue that there is no credible evidence of harm from the Metcalfe letter or Swarovski's late deliveries. Plaintiff was not required to introduce the best possible evidence or all the available evidence to prove its claims. Testimony of retailers that they would not buy Crystal Signatures because of the Metcalfe letter or that they thought less of Ebeling & Reuss after receiving the Metcalfe letter would have been stronger proof of harm to E&R. However, Mr. Russo personally experienced the reaction of retailers after receiving the letter and was competent to testify to the Metcalfe letter's effect. Mr. Russo's testimony about its harm was credible.

Similarly, Mr. Russo was competent to testify to Swarovski's late deliveries of crystal figurines ordered.

Defendants contend that Ms. McKinley's expert testimony rebuts testimony of late deliveries. However, defendants' evidence showed that E&R Co. received "substantial quantities of 22 out of the 44 figurines it ordered." Defendants' Motion for New Trial at 12. That evidence does not contradict Mr. Russo's assertion that Swarovski was delivering late.

Defendants argue that the evidence showed Alco Standard's financial strength was important to Swarovski in deciding to contract with E&R Co. The jury found that the sale of E&R Co. entitled Swarovski to terminate the contract. Defendants further argue that plaintiff introduced no credible evidence of waiver of the right to terminate the contract or failure to notify plaintiff of the termination. The jury could reasonably have found defendants' actions after March 31, 1988 amounted to a refusal to modify the contract, not a termination. *See supra* III.A.1.d.

Defendants moved the court to strike all of Mr. Cook's testimony because of his alleged attempted fraud on the court. Defendants are arguing about Mr. Cook's opinion of Swarovski's value. This opinion was not in evidence; the parties stipulated that Swarovski's net worth was in excess of $200 million; only that stipulation as to value was before the jury. Defendants contend Mr. Cook's method of valuing Swarovski is so inherently flawed that it was intended to deceive the court and therefore tainted all of Mr. Cook's testimony. Mr. Cook readily admitted his method for valuing the Swarovski companies. He never tried to conceal the basis for his opinion from the court. Defendants disagreement with Mr. Cook's methodology in valuing a company is not

relevant to his ability to determine projected profits for a new product line. The court will not strike plaintiff's expert testimony based on an opinion not in evidence.

In arguing for a new trial based on the weight of the evidence defendants understandably ignore their failure to comply with the court's preliminary injunction, affirmed on appeal. The evidence at trial established that defendant offered false and deceptive evidence on impossibility of performance at the preliminary injunction hearing. While refusing to manufacture Disney figurines for Ebeling & Reuss, defendants' manufacturing capacity was utilized to manufacture the Crystal Collectibles product line for Zales in breach of the contract with plaintiff. The jury's verdict on breach of contract, fraud and damages was in accord with the evidence; only a verdict for defendants would have been so against the weight of the evidence that a grant of a new trial would have been warranted.

4. Lack of Notice of Claims

Defendants contend that plaintiff changed its theory of recovery from that in the amended complaint. Defendants argue that they did not have notice of the theories which plaintiff submitted to the jury at trial and thus were severely prejudiced.

a. Plaintiff's pretrial tactics

Defendants accuse plaintiff's counsel of intentionally attempting to obscure its theory of recovery by submitting a pretrial memorandum that was so overinclusive it gave no notice of plaintiff's intentions at trial as required by Local Rule 21(c). Defendants' counsel was therefore unable to focus trial preparation on matters that would be raised at trial.

Plaintiff's pretrial memorandum was 124 pages long, with a 150 page supplemental pretrial memorandum. Even for this long and complicated case, plaintiff's pretrial was overinclusive, but somewhat warranted by defendants' pretrial conduct in changing defense counsel and tactics. Plaintiff certainly was not required to introduce every document and call every witness listed in its pretrial memorandum. Plaintiff should have been able to narrow the witness list and exhibit list by the end of discovery when the pretrial memorandum was due.

However, defendants were not prejudiced by this conduct. Plaintiff's pretrial memorandum explained its theory of the case in its 42 page statement of the facts. Plaintiff listed 41 legal issues to be decided at the trial. Clearly, after a preliminary injunction hearing, and two years of discovery, defendants knew what plaintiff would most likely rely on at trial. Plaintiff called Mr. Russo and Mr. Cook, two witnesses that defendants knew must testify for plaintiff to prove its case. Defendants were obviously prepared to respond to those witnesses.

b. Change in theories

(1) Contract terms

Plaintiff claimed Swarovski breached an exclusive distribution agreement for the product line Crystal Signatures. Defendants argue that in its complaint and pretrial memorandum plaintiff defined product line as those figurines E&R designed or Peter Yenawine designed for E&R. At trial, plaintiff attempted to prove the contract was for all figurines manufactured by Swarovski using the injection molded technology.

Defendants offer no representation made by plaintiff that would limit "product line" in the way defendants suggest. Plaintiff's amended complaint refers to the line of unfaceted injection molded crystal figurines and also to the Crystal Signatures' line. Defendants simply misunderstood what plaintiff meant when it used the term "line." This was not the fault of plaintiff nor due to any ambiguity plaintiff created. Defendants' misunderstanding of plaintiff's use of the word line does not warrant a new trial. Plaintiff made its interpretation clear early in the proceedings and defendants could have rebutted plaintiff's definition; in fact defendants tried to do so.

(2) Draft Written Agreements

Defendants claim plaintiff contended before trial that the draft written agreements were evidence of the terms of the oral agreement, but plaintiff attempted to prove a different contract at trial than that evidenced by the draft written agreements. Plaintiff claimed that inconsistencies between the agreement it was attempting to prove and

the draft agreements were fraudulent attempts by defendants to trick plaintiff into altering the agreement.

At trial, plaintiff's proof of the terms of the contract did not differ entirely from the draft agreements. The parties were negotiating for a new written contract which had been through several revisions. Defendants cite no pretrial statement of plaintiff claiming the contract was exactly the same as the draft agreements. Defendants did not complain of surprise at trial and defendants have not shown how they were harmed.

(3) Assignment of Claim

Defendants contend plaintiff never claimed it was the successor to any claim for pre-March 31, 1988 damages until the middle of trial. The court is at a loss to understand how defendants could not have been on notice of that claim after reading plaintiff's amended complaint and plaintiff's pretrial memorandum. Plaintiff's pretrial memorandum listed the agreement of sale with Alco Standard Corp. as an exhibit. Pl. Pretrial Memorandum at 87. Defendants could have investigated the extent of the assignment by simply reading the contract which was presumably provided during discovery.

Plaintiff clearly demanded damages for pre-March 31, 1988 losses in its amended complaint. The amended complaint is full of references to conduct which occurred in 1985, 1986, and 1987. *See, e.g.*, Amended Complaint at ¶¶ 25, 28, 29, 35, 37, 39, 42, 43, 47, 51, 52, 71, 94. Plaintiff's pretrial memorandum also alleges harm to Ebeling & Reuss Company prior to March 31, 1988. *See* Pl. Pretrial

Memorandum at 5-41. Stressing the claim was unnecessary until new defense counsel contended E&R Ltd. could not assert any rights of E&R Co. Defendants really object that this tactic overlooked the assignment and was ultimately unsuccessful.

(4) Theft of Trade Secrets

Defendants request a new trial on the theft of trade secrets claim because they did not have notice of it prior to trial. However, defendants knew of the evidence supporting that claim and that plaintiff's claim for unfair competition encompassed trade secrets.

At the conclusion of the evidence, plaintiff moved to conform the pleadings to the proof by adding a count for theft of trade secrets. After discussing the motion and the trade secrets claim with the parties, the court stated its view that the trade secrets claim was really just supportive of plaintiff's claim for unfair competition but allowed the jury to answer an interrogatory on the trade secrets claim. The court is still of the view that plaintiff's theft of trade secrets claim was properly before the jury. However, defendants' surprise, if any, is immaterial because the court will enter judgment notwithstanding the verdict on the jury's general finding on unfair competition and disallow damages on the theft of trade secrets claim for the reasons stated above. *See supra* III.A.5&6.

(5) Tortious Interference

Defendants admit that plaintiff claimed SAL interfered with E&R's right to use the Swarovski name. However, they contend it was not until the charging conference that it became clear plaintiff was claiming SAL tortiously interfered with plaintiff's contract with the other defendants. Although the court believes defendants were clearly on notice of the basis for the tortious interference claim, it is immaterial because the court will set aside the tortious interference findings for the reasons stated above. *See supra* III.A.2.

(6) Fraud

Plaintiff's amended complaint and pretrial memorandum complained of Swarovski's fraud in entering the contract without intending to honor it or continuing the contract in order take over the program for its own advantage. All of the fraudulent acts plaintiff claimed at trial related to the fraud alleged prior to trial. Plaintiff was not required to identify separately each individual act of which defendants' alleged fraud was comprised. There was no prejudicial surprise.

(7) Damages

Plaintiff's pretrial memorandum failed to specify the reputation damages and the reliance damages it was claiming. Defendants did not object to the jury interrogatories on those damages. Defendants obviously were not surprised by those demands and cannot come before

the court now asking for a new trial on a technicality that did not prejudice them. Even if there were any surprise, it would be immaterial because the reputation damages will be set aside for the reasons set forth above. *See supra* III.B.2.

c. Notice of Bases of Claims

Defendants claim their counsel was demonstrably confused at trial by plaintiff's change in theories. If defendants' counsel was confused, it was certainly not demonstrable and his confusion, if any, was not caused by plaintiff. Defendants obtained new counsel after plaintiff obtained a preliminary injunction against them, and moved to recuse the judge after that. Now that plaintiff has prevailed at trial, defendants blame the result on defense counsel who was and is an extremely able attorney. The case was vigorously tried by counsel and now the record has been picked apart on behalf of the defense. But this case was not lost by counsel; it was the facts properly in evidence that damaged the defendants. The blame rests not with plaintiff, plaintiff's counsel, plaintiff's witnesses or experts, the judge, confusion of the jury, or defendants' counsel. It was the evidence of defendants' conduct that resulted in this verdict.

d. Erroneous Prejudicial Rulings

(1) Plaintiff's Exhibit 26

Defendants complain that the court precluded defendants from adducing evidence that P-26 came from plaintiff's files. Plaintiff's exhibit 26 was a memorandum from

Peter Yenawine to Helmut Swarovski that listed arguments for Helmut Swarovski to convince the Beirat to allow E&R Co. use of the Swarovski name. When plaintiff originally listed P-26 in its pretrial memorandum, plaintiff identified P-26 as an E&R document. However, at trial, plaintiff identified P-26 as a discovery document produced by Peter Yenawine.

When defendants attempted to cross examine Mr. Russo on P-26, plaintiff's counsel interjected that P-26 was a Peter Yenawine document. Defense counsel objected to the change in identification of the document. Plaintiff's counsel represented to the court that P-26 was a Peter Yenawine document received by plaintiff in document production prior to the preliminary injunction hearing and initially misidentified as coming from E&R's files. The court was entitled to rely on this representation from an officer of the court; the court did not improperly limit defendants use of P-26.

Later in the proceedings, the court gave a limiting instruction to the jury that the statements in P-26 could not be used against plaintiff unless the jury found that Mr. Russo had knowledge of the contents of P-26 prior to the litigation. Defendants argue that plaintiff could be charged with knowledge of P-26 if anyone at E&R Co. or Alco Standard knew of its contents at the time the E&R – Swarovski relationship was beginning. If defendants had any evidence that anyone else from E&R or Alco Standard knew of P-26, defendants could have asked the court for a curative instruction to the jury. Defendants did not introduce any such evidence nor did they object to the court's instruction. This jury instruction does not require a new trial.

(2) Plaintiff's Exhibit 12

Defendants complain that Mr. Russo was allowed to give his opinion of the meaning of the words in P-12 but defendants' witness, Kurt Mignon, the author of P-12, was not allowed to testify about his understanding of the meaning.

Mr. Russo was allowed to testify to his understanding of the terms in P-12. Mr. Mignon was also allowed to testify to his understanding of the agreement. The court correctly stated that Mr. Mignon could not state what the exhibit itself said because the letter spoke for itself. The court's ruling was not erroneous.

D. MOTION FOR DISQUALIFICATION

On October 18, 1989, defendants filed a Motion for Disqualification pursuant to 28 U.S.C. §144 and §455. On October 24, 1989, plaintiff filed its answer in opposition to the defendants' motion. On January 30, 1990, the court denied defendants' motion and stated its reasons to the parties; a written statement of the reasons for denying defendants' motion has not yet been filed and follows.

In *Mims v. Shapp*, 541 F.2d 415 (3d Cir. 1976), the Court of Appeals held that a district judge faced with a motion for disqualification under 28 U.S.C. §144, must accept the allegations of the moving party as true, stating:

> On such a motion it is the duty of the judge to pass only on the legal sufficiency of the facts alleged to ascertain whether they support a charge of bias or prejudice. Neither the truth of the allegations nor the good faith of the pleader

> may be questioned, regardless of the judge's knowledge to the contrary. The test is whether, assuming the facts alleged, a reasonable person would conclude that a personal as distinguished from a judicial bias exists.

541 F.2d at 417 (citations omitted). Once the allegations of the moving party are accepted, the Court of Appeals has made clear that a judge is disqualified only for extrajudicial bias. *Johnson v. Trueblood,* 629 F.2d 287, 290-91 (3d Cir. 1980), *cert. denied,* 450 U.S. 999 (1981).

> "Extrajudicial bias" refers to a bias that is not derived from the evidence or conduct of the parties that the judge observes in the course of proceedings. *See United States v. Grinnell Corp.,* 384 U.S. 563, 580-82, . . . (1966). Normally, the judge's rulings at trial do not constitute grounds for recusal because they can be reversed on appeal. *See Smith v. Danyo,* 585 F.2d 83, 87 (3d Cir. 1978).

Id. at 291. "The relevant inquiry is whether the trial judge's comments are linked to [her] evaluation of the case . . . or whether the comments were based on purely personal feelings towards the parties and the case." *Id.* Both 28 U.S.C. §144 and §455 require the same type of bias for recusal. *Id.* at 290.

Defendants claimed it was improper for the court at a pretrial status conference to question defendants' former counsel on whether there were laws against involuntary servitude in Austria, Switzerland, and Liechtenstein, after defendants' counsel suggested that the countries (where conduct relevant to conduct at issue occurred) might have constitutional provisions or laws equivalent

to our Thirteenth Amendment. It is not evidence of extra-judicial bias for the court to question whether such laws exist in the absence of proof. *See* Fed. R. Civ. P. 44(a)(2) and 44.1. After defense counsel could not answer the court's question, the court replied that maybe those countries had in recent years adopted such laws. Defendants assert that the court's answer to its own query "doubtless refer[s] to the past." Defendants' Brief at 7.

Defendants' brief refers obliquely to the gist of defendants' argument – that this court is prejudiced against these Austrian, Swiss, Liechtenstein, and American defendants because of something that happened in the past and that this court's comments showed bias regarding defendants' nationalities. While the court's comment may have been somewhat irrelevant, it was responsive to remarks of defense counsel and was sufficiently related to the proceedings not to warrant recusal. *See, e.g., United States v. Crovedi,* 467 F.2d 1032, 1039-40 (7th Cir. 1972), *cert. denied,* 410 U.S. 982 (1973); *Senchal v. Carroll,* 394 F.2d 797, 799 (10th Cir.), *cert. denied,* 393 U.S. 979 (1968).

Defendants next complained that the record for the same conference reveals that plaintiff's counsel "appears to have attempted to influence the Court by appealing to prejudice based on the nationality of the defendants." Defendants' Brief at 3. In the colloquy cited, it is clear that the court was tired of plaintiff's counsel's use of the term "red herring" to describe defendants' challenge to the court's jurisdiction and that the court was concerned by (indeed, struck from the record) plaintiff's facetious comments about the former Austrian flag. If plaintiff's

counsel were intending to influence the court, the record shows clearly that the court was unmoved. Again, the judge's words on that occasion have nothing to do with its view of the parties or the merits.

Defendants also complained of the court's comment in considering discovery matters that the defendants might not understand or like the litigation process in the United States. As the Court of Appeals noted in *Johnson*, a district judge often can get a feel for a case prior to trial, so that feelings can be based on the conduct of the parties and the evidence. "The relevant inquiry is whether the trial judge's pretrial comments were linked to his evaluation of the case based on the pleadings and other materials outlining the nature of the case, or whether the comments were based on purely personal feelings toward the parties and the case." *Id.* at 291. This comment clearly reflected the court's view of defendants' conduct in this litigation during extended discovery, preliminary hearings, and attempts to encourage settlement negotiations between the parties; it did not reflect personal views or biases.

Defendants complain of the court's personal bias in questioning whether two defense witnesses who testified at prior hearings had been found to be liars. The defendants had failed to comply with a preliminary injunction of July 30, 1988, the issuance of which was affirmed by the Court of Appeals, 866 F.2d 1409 (3d Cir. 1988). The court reserved judgment and deferred ruling, following a contempt hearing on September 14, 15 and October 6, 1988, pending a full presentation of the evidence at trial. Nevertheless, the court had obtained enough information to make a credibility assessment as the finder of fact at

non-jury proceedings; the statement at the subsequent pretrial discovery conference on September 6, 1989, was an evaluation of the credibility of witnesses the court had heard testify. This evaluation was confirmed by the trial record; in any event, it was not improper under *Johnson*.

Finally, defendants argue that the court's discovery rulings amount not only to an abuse of discretion but to evidence of actual bias on the part of the court. The court's decision to enter a scheduling order "to insure the resolution of this dispute in a timely manner . . . do[es] not constitute personal or extrajudicial statements or actions by the court, but rather, concerns actions taken by the court after examining the evidence and legal precedent. Actions taken after reviewing the applicable legal standards and evidentiary record, as opposed to extrajudicial actions, will not support recusal." *Grand Entertainment Group, Ltd. v. Arazy*, 676 F. Supp. 616, 619 (E.D. Pa 1987).

Defendants' complaint of bias in the court's decision in September, 1989 to order that depositions take place in the United States or that defendants pay plaintiff's counsel to go to Europe fails to account for a district judge's power to "make any order which justice requires to protect a party or person from . . . or undue burden or expense." Fed. R. Civ. P. 26(c). The defendants fail to acknowledge that the Order followed preliminary injunction hearings and contempt hearings at which the court gained an understanding of defendants' business and business practices; the court held a conference with full consideration of discovery issues to help the court decide what was fair and reasonable in the circumstances. District courts have broad discretion in trial management

under Fed. R. Civ. Pro. 26(c). *Afram Export Corp. v. Metallurgiki Halyps, S.A.*, 772 F.2d 1358, 1365 (7th Cir. 1985), and its exercise is not ground for recusal.

The filing of a motion of recusal accompanied by an affidavit by an attorney does not automatically disqualify the target judge. *Grand Entertainment Group, Ltd.*, 676 F. Supp. at 619. To the contrary, "[w]hile the judge has an affirmative duty to disqualify himself should the affidavit set forth sufficient allegations concerning bias, the judge has an equally affirmative duty to retain the case should the affidavit lack sufficient allegations or fail to generate a reasonable doubt concerning the judge's impartiality." *Id.* Defendants allegations did not meet the definition of extrajudicial bias required to support a motion for recusal; new counsel for the defendants simply searched the record for a reason to disqualify the judge who had ruled against the defendants in preliminary matters. For that reason, it would have been improper to grant defendants' motion on the grounds stated above.

IV. PLAINTIFF'S MOTIONS

A. New Trial

Plaintiff conditionally moved for a new trial on damages in the event defendants were granted a new trial on any issue. Since the court has denied defendants' motion for a new trial on any issue, plaintiff's motion for a new trial is deemed withdrawn.

B. Amend Verdict

Plaintiff moved the court to amend the verdict to award nominal damages on its trademark and unfair competition claims. The jury found in favor of plaintiff on the trademark and unfair competition claims but failed to award plaintiff any additional compensatory damages. (*See* Appendix C) Since the court has granted judgment notwithstanding the verdict on those counts, the verdict will not be amended to reflect nominal damages.

C. Additur on Punitive Damages

Plaintiff, moving for additur on the punitive damages, claims defendants fraudulently concealed their true net worth. During the trial, after some disagreement on the offer of proof on Mr. Cook's opinion of Swarovski's net worth, the parties stipulated that Swarovski's net worth was in excess of $200 million. Plaintiff claims defendants' true worth is in excess of $2 billion, ten times greater than the figure the jury considered; therefore, the punitive damages should also be increased by a factor of ten.

Defendants' financial worth was the subject of much discussion during the trial. The parties were given the option of delaying determination of punitive damages until the parties could conduct discovery on defendants' financial worth. Both parties agreed to proceed with the trial without further delay by stipulating that defendants financial worth was in excess of $200 million. Plaintiff made a tactical decision at the time to continue with a jury that had already ruled favorably for Ebeling &

Reuss. The court questions its authority to add to a jury verdict and would decline to do so even if it had the power. Plaintiff's motion for additur will be denied.

D. Motion for Contempt

The court heard argument on the motion for contempt but reserved ruling on the motion until after the trial. Following the trial, the parties requested that the court defer ruling on the motion for contempt until after the post trial motions were decided. Plaintiff will be given the opportunity to inform the court whether it wishes to proceed with the motion for contempt.

E. Motions for Attorneys' Fees

Plaintiff filed a motion for attorneys' fees in connection with its trademark claims and a motion for attorneys' fees in connection with the contempt proceedings. Since the court granted judgment notwithstanding the verdict on the trademark claims, plaintiff is not entitled to recover attorneys' fees for prosecuting that claim.

The motion for attorneys' fees for the contempt proceedings will be deferred until decision on the motion for contempt.

V. CONCLUSION

For the foregoing reasons, defendants' motion for judgment notwithstanding the verdict will be granted in part and denied in part, defendants' motion to alter or

amend the verdict will be granted in part and denied in part, and defendants' motion for a new trial will be denied.

Plaintiff's motion for a new trial will be deemed withdrawn; plaintiff's motions to amend the verdict, for additur, and for attorneys' fees on the trademark claims are denied. Plaintiff shall promptly inform the court whether it wishes to pursue the motions for contempt and attorneys' fees for the contempt claim.

An appropriate order follows.

APPENDIX A

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

EBELING & REUSS, LTD. t/a EBELING & REUSS COMPANY	:	CIVIL ACTION
v.	:	(Filed June 2, 1990)
SWAROVSKI INTERNATIONAL TRADING CORPORATION, A.G., individually and d/b/a D. SWAROVSKI & CO. and SWAROVSKI AMERICA LIMITED and SWAROVSKI AKTIENGELSELLSCHAFT	:	NO. 88-4878 MICHAEL E. KUNZ, Clerk By /s/ Dep. Clerk

SPECIAL INTERROGATORIES TO THE JURY

A. Contract:

1. Has plaintiff proved by a preponderance of the evidence that the course of dealings between the Ebeling & Reuss Division of Alco Standard Corporation and the Swarovski defendants created an enforceable contract that the Swarovski defendants breached?

Yes X No _

2. If your answer to interrogatory 1 was "yes," has plaintiff proved by a preponderance of the evidence that a breach of contract prior to March 31, 1988 caused harm to the Ebeling & Reuss Division of Alco Standard Corporation?

Yes X No _

3. If your answer to interrogatory 1 was "yes," has plaintiff proved by a preponderance of the evidence

that a breach occurred after March 31, 1988 that caused harm to Ebeling & Reuss, Ltd.?

Yes X No _

4. If your answer to interrogatory 3 was "yes," have the Swarovski defendants proved by a preponderance of the evidence that the sale of the Ebeling & Reuss Division of Alco Standard Corporation and incorporation of Ebeling & Reuss, Ltd. entitled the Swarovski defendants to terminate the contract?

Yes X No _

5. If your answer to interrogatory 4 was "yes,"

   a. Did the Swarovski defendants inform Ebeling & Reuss, Ltd. of the termination?

   Yes _ No X

   or

   b. Has plaintiff proved by a preponderance of the evidence that the Swarovski defendants waived a right to terminate the contract?

   Yes X No _

6. If your answer to interrogatory 4 or 5a was "no," or if your answers to interrogatory 4 and 5b were "yes," has plaintiff proved by a preponderance of the evidence that a breach of contract subsequent to March 31, 1988 caused harm to Ebeling & Reuss, Ltd.?

Yes X No _

B. Promissory Estoppel:

1. Has plaintiff proved by a preponderance of the evidence that the Swarovski defendants made certain promises to the Ebeling & Reuss Division of Alco Standard Corporation concerning the manufacture, packaging and sale of injection molded crystal miniature figurines called Crystal Signatures that were breached by the defendants?

Yes X No _

2. If your answer to interrogatory 1 was "yes," has plaintiff proved by a preponderance of the evidence that the Ebeling & Reuss Division of Alco Standard Corporation acted in a reasonable reliance on these promises?

Yes X No _

3. If your answer to interrogatory 2 was "yes," has plaintiff proved by a preponderance of the evidence that the Ebeling & Reuss Division of Alco Standard Corporation was injured by the Swarovski defendants' breach of promises?

Yes X No _

4. If your answer to interrogatory 1 was "yes," has plaintiff proved by a preponderance of the evidence that Ebeling & Reuss, Ltd. acted in reasonable reliance on these promises?

Yes X No _

5. If your answer to interrogatory 4 was "yes," have defendants proved by a preponderance of the evidence that the sale of the Ebeling & Reuss Division of Alco Standard Corporation and incorporation of Ebeling & Reuss, Ltd. on March 31, 1988 excused the

Swarovski defendants from performance of their promises?

Yes _ No X

6. If your answer to interrogatory 5 was "yes," has plaintiff proved by a preponderance of the evidence that the Swarovski defendants waived the excuse so that the promises remained enforceable after the take-over?

Yes _ No _

C. Tortious Interference With Contract:

1. Has plaintiff proved by a preponderance of the evidence that Swarovski America Limited caused harm to the Ebeling & Reuss Division of Alco Standard Corporation by wrongfully interfering with its existing or prospective contractual relations with the other Swarovski defendants?

Yes X No _

2. Has plaintiff proved by a preponderance of the evidence that Swarovski America Limited caused harm to Ebeling & Reuss, Ltd. by wrongfully interfering with the existing or prospective contractual relations with the other Swarovski defendants?

Yes X No _

3. Has plaintiff proved by a preponderance of the evidence that any of the following defendants caused harm to the Ebeling & Reuss Division of Alco Standard Corporation by wrongfully interfering with its existing or prospective contractual relations with people or businesses other than the Swarovski defendants:

Swarovski International Trading Corporation, A.G. individually and doing business as D. Swarovski & Co.

Yes X No _

Swarovski America Limited

Yes X No _

Swarovski Aktiengelsellschaft

Yes _ No X

4. Has plaintiff proved by a preponderance of the evidence that any of the following defendants caused harm to Ebeling & Reuss, Ltd. by wrongfully interfering with its existing or contractual relations with people or businesses other than the Swarovski defendants:

Swarovski International Trading Corporation, A.G. individually and doing business as D. Swarovski & Co.

Yes X No _

Swarovski America Limited

Yes X No _

Swarovski Aktiengelsellschaft

Yes _ No X

D. Fraud:

1. Has plaintiff proved by clear, precise and convincing evidence that any Swarovski defendant(s) intentionally misrepresented or intentionally failed to disclose a material fact with the intent to deceive the Ebeling & Reuss Division of Alco Standard Corporation?

Yes X No _

If your answer to interrogatory 1 was "yes," please answer interrogatory 2.

If your answer to interrogatory 1 was "no," please answer interrogatory 3.

2. Has plaintiff proved by clear, precise and convincing evidence that the Ebeling & Reuss Division of Alco Standard Corporation's justifiable reliance on this misrepresentation or failure to disclose caused it harm?

Yes X No _

Please answer interrogatory 3.

3. Has plaintiff proved by clear, precise and convincing evidence that any Swarovski defendant(s) intentionally misrepresented or intentionally failed to disclose a material fact with the intent to deceive Ebeling & Reuss, Ltd.?

Yes X No _

If your answer to interrogatory 3 was "yes," please answer interrogatory 4.

If your answer to interrogatory 3 was "no," please go to page 5.

4. Has plaintiff proved by clear, precise and convincing evidence that Ebeling & Reuss, Ltd.'s justifiable reliance on this misrepresentation or failure to disclose caused it harm?

Yes X No _

E. Conspiracy:

1. Has plaintiff proved by full, clear and satisfactory evidence that any of the following defendants conspired with each other to injure the Ebeling & Reuss Division of Alco Standard by wrongful interference with its existing or prospective contractual relations or by fraud:

   Swarovski International Trading Corporation, A.G. individually and doing business as D. Swarovski & Co.

   Yes X No _

   Swarovski America Limited

   Yes X No _

   Swarovski Aktiengelsellschaft

   Yes _ No X

2. Has plaintiff proved by full, clear and satisfactory evidence that any of the following defendants conspired with each other to injure Ebeling & Reuss, Ltd. by wrongful interference with its existing or or prospective contractual relations or by fraud:

   Swarovski International Trading Corporation, A.G. individually and doing business as D. Swarovski & Co.

   Yes X No _

   Swarovski America Limited

   Yes X No _

   Swarovski Aktiengelsellschaft

   Yes _ No X

/s/
Foreperson

Date: 6/18/90

PLEASE NOTIFY THE DEPUTY CLERK WHEN YOUR DELIBERATIONS HAVE CONCLUDED.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

EBELING & REUSS, LTD. t/a EBELING & REUSS COMPANY	:	CIVIL ACTION (Filed 1990)
v.	:	
SWAROVSKI INTERNATIONAL TRADING CORPORATION, A.G., individually and d/b/a D. SWAROVSKI & CO. and SWAROVSKI AMERICA LIMITED and SWAROVSKI AKTIENGELSELLSCHAFT	:	NO. 88-4878

SPECIAL INTERROGATORIES TO THE JURY

1. In what amount, if any, has plaintiff proved by a preponderance of the evidence that plaintiff suffered monetary loss as a result of defendants' conduct?

	Ebeling & Reuss Div. of Alco Standard Corp.	Ebeling & Reuss, Ltd.	or Plaintiff
Actual Damages	$	$	$850,000
Lost Profits	$	$	$ 25 million
Harm to Reputation	$	$	$ 8 million
TOTAL	$	$	$33,850 million

2. In what amount, if any, has plaintiff proved by a preponderance of the evidence that it is entitled to punitive damages?

Ebeling & Reuss Division of Alco Standard Corp.	Ebeling & Reuss, Ltd.	or	Plaintiff
$	$		$16.5 million

Date: 6/19/90

/s/
Foreperson

PLEASE NOTIFY THE DEPUTY CLERK WHEN YOUR DELIBERATIONS ARE FINISHED.

APPENDIX C

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

EBELING & REUSS, LTD. t/a EBELING & REUSS COMPANY	:	CIVIL ACTION (Filed 1990)
v.	:	
SWAROVSKI MANAGEMENT & CONSULTING A.G. and D. SWAROVSKI & CO. and SWAROVSKI AMERICA LIMITED and SWAROVSKI AKTIENGESELLSCHAFT and SWAROVSKI INTERNATIONAL TRADING CORPORATION	:	NO. 88-4878

SPECIAL INTERROGATORIES TO THE JURY

A. Trademark

1. Has plaintiff proved by a preponderance of the evidence that similarity between the name, "Crystal Collectibles," and plaintiff's trademark, "Crystal Signatures," was likely to cause confusion or mislead consumers into believing that the products came from the same source?

Yes X No _

B. Unfair Competition

2. Has plaintiff proved by a preponderance of the evidence that defendants copied the trade dress of plaintiff's "Crystal Signatures"?

Yes X No _

3. Has plaintiff proved by a preponderance of the evidence that plaintiff's trade dress acquired a secondary meaning in the marketplace because it

identified "Crystal Signatures" in consumers' minds as belonging to plaintiff?

Yes X No _

4. Has plaintiff proved by a preponderance of the evidence that defendants created a likelihood of confusion among consumers as to the source of the product by imitation of plaintiff's trade dress?

Yes X No _

C. 5a. Of plaintiff's lost profits in the amount of $25 million, what amount, if any, resulted from the acts of defendants in marketing and selling the "Crystal Collectibles" line through Zales Corporation?

$ Zero

5b. In what amount, if any, has plaintiff proved by a preponderance of the evidence that it is entitled to additional punitive damages for the acts of defendants in marketing and selling the "Crystal Collectibles" line through Zales Corporation?

$2.5 million

D. Misappropriation of Trade Secret

6. Has plaintiff proved by a preponderance of the evidence that defendants wrongfully used a trade secret of plaintiff which caused harm to plaintiff?

Yes X No _

E. Damages

7a. In what amount, if any, has plaintiff proved by a preponderance of the evidence that defendants

profited as a result of their misappropriation of trade secret?

$291,345.–

7b. In what amount, if any, has plaintiff proved by a preponderance of the evidence that it is entitled to additional punitive damages for defendants' misappropriation of trade secret?

$2.5 million

Date: 6/21/90 /s/
Foreperson

PLEASE ADVISE THE DEPUTY CLERK WHEN YOUR DELIBERATIONS HAVE CONCLUDED.

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

EBELING & REUSS, LTD. t/a EBELING & REUSS COMPANY,	:	CIVIL ACTION
v.	:	
SWAROVSKI INTERNATIONAL TRADING CORPORATION, A.G., individually and d/b/a D. SWAROVSKI & CO. and SWAROVSKI AMERICA LIMITED and SWAROVSKI AKTIENGELSELLSCHAFT	:	NO. 88-4878

ORDER

AND NOW, this 24th day of August, 1992, upon consideration of: defendants' motion for a new trial, motion for judgment notwithstanding the verdict, and motion to alter or amend the verdict; and, plaintiff's conditional motion for a new trial, motion to amend the verdict, motion for additur, motion for contempt, motion for attorneys' fees on the trademark claim, and motion for attorneys' fees on the contempt claim, it is **ORDERED** that:

1. Defendants' motion for a new trial is **DENIED.**

2. Defendants' motion for judgment notwithstanding the verdict is **GRANTED IN PART** and **DENIED IN PART** as follows:

a. Judgment for plaintiff and against defendants for tortious interference is set aside.

b. Judgment for plaintiff and against defendants for fraud for intentionally misrepresenting or intentionally failing to disclose a material fact with the intent to deceive Ebeling & Reuss, Ltd. is set aside.

c. Judgment for plaintiff and against defendants on the trademark, unfair competition, and trade secret claims is set aside.

d. The damage award under trademark and unfair competition for the acts of defendants in marketing and selling the "Crystal Collectibles" line through Zales Corporation is set aside.

3. Defendants' motion to alter or amend the verdict is **GRANTED IN PART** and **DENIED IN PART** as follows:

a. The damage award for reputation damages is set aside.

b. The damage award for defendants' profit for misappropriation of trade secret is set aside.

c. The punitive damages awards for trademark, unfair competition, and trade secret are set aside.

d. The court will mold the verdict and enter judgment in favor of plaintiff and against defendants in the total amount of $42,350,000.

4. Plaintiff's conditional motion for a new trial is **DEEMED WITHDRAWN.**

5. Plaintiff's motion to amend the verdict is **DENIED.**

6. Plaintiff's motion for additur is **DENIED.**

7. Plaintiff's motion for attorneys' fees for the trademark claim is **DENIED.**

8. Plaintiff shall inform the court by **September 8, 1992** if it wishes to pursue its motions for contempt and attorneys' fees for the contempt claim.

/s/ Norma L. Shapiro
J.

Nos. 92-1723 and 92-1746

IN THE UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

SWAROVSKI INTERNATIONAL TRADING CORPORATION, A.G., et al., APPELLANTS and CROSS-APPELLEES

v.

EBELING & REUSS, LTD. t/a EBELING & REUSS COMPANY, APPELLEE and CROSS-APPELLANT

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

HONORABLE NORMA SHAPIRO, UNITED STATES DISTRICT JUDGE

PETITION FOR REHEARING AND REHEARING IN BANC

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I. SUMMARY OF ARGUMENT AND PROCEEDINGS

A. Propriety Of In Banc Review.

Pursuant to Federal Rules of Appellate Procedure 35 and 40, the Appellants and Cross-Appellees here, Defendants below,[1] respectfully move this Court for rehearing and rehearing in banc of the April 7, 1993 Judgment Order in No. 92-1746 affirming the $42,350,000 judgment of the district court against Defendants. Swarovski petitions for rehearing in banc understanding the Court's advice that, "except in rare cases," rehearing in banc is not granted where an appeal was decided by judgment order. Third Circuit Internal Operating Procedures ("IOP"), Ch. 9. They nevertheless make that request here precisely because this is one of those rare instances in which the device of the judgment order has been improperly used to endorse a judgment entered in violation of controlling decisions of this Circuit with respect to (1) the right to terminate a contract of indefinite duration, (2) the applicability of the Statute of Frauds to distribution agreements, and (3) the legal standard of proof of lost profits damages. The Court's disposition of Swarovski's appeal has also created a conflict with the law of other Circuits concerning the right of a court to apportion punitive damages among particular causes of action when the jury did not apportion them and when certain of the tort claims did not survive review. Further, by

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[1] The Defendants, Appellants in No. 92-1746, are Swarovski Management & Consulting, A.G., D. Swarovski & Company, Swarovski Atkiengesellscaft, Swarovski America Limited, and Swarovski International Trading Corporation, A.G., all of which are hereafter referred to as "Swarovski."

employing the device of the judgment order to confirm a judgment which includes an award of $16.5 million in punitive damages – some 8.25% of Defendants, stipulated net worth – the Court has failed in its constitutionally mandated task to review the punitive damage award under the Supreme Court's decision in *Pacific Mut. Life Ins. Co. v. Haslip*, 111 S. Ct. 1302 (1991).[2]

B. Summary Of Prior Proceedings.

The instant case arose out of an alleged exclusive distribution contract between Ebeling & Reuss Limited ("E&R"), an American company engaged in the business of distributing and marketing giftware in the United States, and the largely Austrian based Swarovski Defendants, who are engaged in the manufacture of fine crystal. See App. 2645a. At trial, E&R contended that a series of oral and written communications in late 1985 and early 1986 culminated in an agreement granting E&R the exclusive right to distribute all miniature crystal figurines manufactured by Swarovski's injection molding technology. *See* App. 1776a; 4346a. Although the parties exchanged drafts of a comprehensive written agreement during this time, *see* App. 1979a; 4105-71a; 4140-52a; 4555-64a, it is undisputed that no version of the draft contracts was ever agreed to or executed. During this period, Swarovski filled E&R's purchase orders for the crystal figurines, which E&R marketed under the name

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[2] *See also Dunn v. Hovic*, 1992 U.S. App. LEXIS 22749, 1992 WL 22875 (3d Cir., Sept. 18, 1992) (No. 91-3837), *rehearing granted and opinion vacated* (October 8, 1992).

"Crystal Signatures." However, when the written agreement did not materialize and E&R was sold in a leveraged buyout, Swarovski terminated its relationship with E&R. App. 4396a. Following this termination, E&R filed the instant suit against Swarovski, alleging, *inter alia*, claims for breach of contract and fraud. *See* App. 100a-179a.

At trial, E&R's case consisted primarily of the testimony of Michael Russo, one of its owner/officers, and Stephen Cook ("Cook"), its damage expert. At the conclusion of the trial, the jury rendered a verdict in favor of E&R on all claims, awarding it $34,141,364 in compensatory damages and $21,500,000 in punitive damages. On June 22, 1990, the district court entered judgment on the verdict in the amount of $55,641,364.

Following the entry of judgment, all parties timely filed post-trial motions. The district court ruled on these motions on August 25, 1992, setting aside jury findings on several of Plaintiff's claims, but upholding the jury's findings of liability on breach of contract and on one of the fraud claims. *See* App. 1394a-1477a. The court then entered final judgment against Swarovski in the amount of $42,350,000, consisting of $850,000 in out-of-pocket expenses, $25,000,000 in lost profits, and $16,500,000 in punitive damages. *Id.* It was this judgment that the Panel summarily affirmed by a Judgment Order on April 7, 1993.

II. ARGUMENT

A. THE PANEL MISCONSTRUES THE LAW OF THIS CIRCUIT IN AFFIRMING THE AWARD OF $25 MILLION IN LOST PROFITS ON A CONTRACT OF INDEFINITE DURATION.

E&R's owner/officer testified that the alleged distribution agreement was to continue for "the life of the product cycle," that is, "for as long as the merchandise was selling in the market." App. 1856a. Such an agreement is, as a matter of law, one of indefinite term. *See Excello Wine Co. v. Monsieur Henri Wines, Ltd.*, 474 F. Supp. 203 (S.D. Ohio 1979) (a distributorship contract to last as long as "mutually profitable" was held to be indefinite); *Universal Lite Distribs., Inc. v. Northwest Indus., Inc.*, 602 F.2d 1173, 1175 (4th Cir. 1979) (an oral agreement to last as long as the parties remained in the ballast business was held to be "indefinite in duration"). Consequently, the contract was terminable at will on reasonable notice, *see* 13 Pa. Cons. Stat. Ann. § 2309 (1980); *Weilerbacher v. Pittsburgh Brewing Co.*, 218 A.2d 806, 807 (Pa. 1966), a legal proposition which the trial court failed to comprehend, refusing to give Swarovski's requested instruction in that regard, *see* App. 893a, and erroneously charging the jury that the contract could be given some "reasonable" term of years in direct contravention of the U.C.C. *Compare* 13 Pa. Cons. Stat. Ann. § 2309 *with* App. 3397-98a (charge). *See also* 979a (Memorandum in Support of Motion for Directed Verdict). The error went to the heart of the entire case and would obviate almost all of the $42 million in damages because a terminable-at-will distributorship contract can only support a damage award for

the time necessary to find a new source of supply.[3] Yet no court *at any level of these proceedings* has ever addressed this issue!

The Panel's decision has also totally misapplied a line of Third Circuit decisions which holds that where an agreement is *silent* on duration, the intention of the parties on that point is to be gleaned from the surrounding circumstances and the contract as a whole.[4] Those cases have no application here because instead of being silent the contract in this case contained an express term of duration which was inherently indefinite. Accordingly, the order of affirmance in this case is contrary to the UCC and totally at odds with earlier decisions of this Court.

B. THE PANEL DECISION VIOLATES THE HOLDING OF THIS COURT IN *ADVENT SYSTEMS LTD.* ON THE REQUIREMENTS NEEDED FOR A DISTRIBUTION AGREEMENT TO SATISFY THE STATUTE OF FRAUDS.

In its decision in *Advent Systems Ltd. v. Unisys Corp.*, 925 F.2d 670 (3d Cir. 1991), this Court held that a distribution agreement could satisfy the Pennsylvania Statute of

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[3] *See* Pa. Cons. Stat. Ann. § 2309, comment 8; *Jo-Ann, Inc. v. Alfin Fragrances, Inc.*, 731 F. Supp. 149, 160 (D.N.J. 1989); *Circo v. Spanish Gardens Food Mfg. Co.*, 643 F. Supp. 51, 54-55 (W.D. Mo. 1985).

[4] *Institute for Scientific Info., Inc. v. Gordon & Breach, Science Publishers, Inc.*, 931 F.2d 1002, 1009 n.8 (3d Cir.), *cert. denied*, 112 S. Ct. 302 (1992); *Von Lange v. Morrison-Knudsen Co., Inc.*, 460 F. Supp. 643 (M.D. Pa.), *aff'd*, 609 F.2d 504 (3d Cir. 1979); *American Type Founders v. Lanston Monotype Mach. Co.*, 137 F.2d 728 (3d Cir. 1943).

Frauds, despite the absence of any written quantity term, provided there existed a detailed *written* agreement which would "leave no doubt" that the parties intended to create the distribution arrangement. This Court specifically declined the invitation to hold that lost profits damages could be recovered on an alleged distribution agreement where a detailed writing was lacking.

In conflict with the *Advent* decision, the Panel has affirmed the award of $25 million in lost profits damages for breach of a claimed distribution agreement where the writings identified by the proponent of the agreement are wholly insufficient to demonstrate such a definitive, long-term contract. *See* 3863-66a; 3877-86a; 3904a. In its emphasis on the detailed nature of the writing at issue, *Advent* teaches that, in order to satisfy the Statute of Frauds, E&R must have *in writing* sufficient details to demonstrate that the contract between the parties is in fact an exclusive distribution contract obligating Swarovski to satisfy E&R's requirements.[5] None of the terms identified by this Court in *Advent* are present in the writings here. To the contrary, it is undisputed that the writings in this case are silent on the basic and fundamental terms of the overall relationship, such as duration, termination and quantity of orders. *See* App. 3863a; 3865-66a; 3877-82a; 3885-86a; and 3904a (relied on by E&R to satisfy the Statute of Frauds).

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[5] *See also Eastern Dental Corp. v. Isaac Masel Co.*, 502 F. Supp. 1354, 1363-64 (E.D. Pa. 1980); *Zayre Corp. v. S.M. & R. Co.*, 88 F.2d 1145, 1155 (7th Cir. 1989).

C. THE AWARD OF $25 MILLION IN LOST PROFITS DAMAGES IS VIOLATIVE OF WELL-ESTABLISHED AND WELL-REASONED THIRD CIRCUIT LAW ON THE LEGAL STANDARD FOR PROOF OF DAMAGES.

In two recent opinions, *Tunis Bros. Co. v. Ford Motor Co.*, 952 F.2d 715 (3d Circuit), *cert. denied*, 112 S. Ct. 3034 (1992) and *Advent Systems, Ltd. v. Unisys Corp.*, 925 F.2d 670 (3d Cir. 1991), this Court has substantially redefined the law regarding awards of lost profits damages. In these decisions, the Court has clearly held that a party may not recover lost profits for a period of time greater than the underlying contract and that reliance on expert testimony in lieu of actual figures, especially when based on a plaintiff's own pre-contract profit projections, are disfavored. Both of those standards were utterly abandoned in this case.

1. Plaintiff's Expert Protected Profits For A Period Of Time Beyond The Contract Term In Violation of Controlling Third Circuit Precedent.

The $25 million lost profits award is erroneously based on ten year projections of sales for both the Crystal Signatures and Disney[6] lines. *See* App. 4527a. *See also* App. 2373a. E&R's contract with Disney provided for a duration of three years, with a highly contingent one year

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[6] At trial, E&R successfully asserted that Swarovski had agreed to extend the exclusive distribution contract with E&R to include a line of injection-molded miniature crystal Disney figurines.

option. App. 4127a-39a (Disney contract). Nonetheless, E&R's expert projected profits on the Disney line for a full ten years. *See* App. 4527a. In *Tunis Bros.*, this Court clearly held that a plaintiff may not recover lost profits for a period of years greater than the duration of the contract on which those profits are premised. 952 F.2d at 735. Accordingly, the Panel's affirmance of the award of lost profits for a period of ten years is contrary to *Tunis Bros.*, and should be reversed.

2. Plaintiff's Expert Disregarded Actual Sales Figures In Violation Of The Prior Admonitions Of This Court.

The Third Circuit has joined the growing list of circuits that has recognized and spoken out against the "old problem of expert witnesses." *Advent*, 925 F.2d at 682 (citations omitted). In *Advent*, the plaintiff's expert testified that total industry sales of a computer program product would have been $77 and $255 million in 1987 and 1988, notwithstanding actual sales of $12 million and $10 million, respectively, for those years. Although the expert in *Advent* stopped short of admitting that he ignored actual figures, in the absence of any other explanation, the Court presumed that the expert disregarded actual sales because of the defendants' conduct, an explanation which the *Advent* Court found to be "unconvincing at best." *Id.* The *Advent* Court then held that the expert's testimony was completely speculative in the light of actual sales, and issued the following admonition:

> We too have serious reservations about the validity of expert testimony on prior predictions of

> sales for a given period when actual performance data for that same time span are available.

Id.

This admonition was completely ignored in this case. Surpassing even the plaintiff's expert in *Advent*, Cook *admitted* that he disregarded actual sales results in formulating his projections. *See* App. 2324a. Accordingly, for the years 1987-1989, Cook adopted E&R's sales projections of $5 million, $10 million, and $13 million, respectively, App. 2375a, notwithstanding actual sales of $669,000.00, $281,000.00, and $550,000.00 in those years. App. 4527a. *See also* App. 2332-33a. Cook's rejection of actual figures and his refusal even to factor them into his calculation of damages is erroneous under this Court's decision in *Advent*.

3. Plaintiff's Expert Relied On And Extended Plaintiff's Pre-Contract Sales Projections In Contravention Of The Holding Of This Court.

Cook based his lost profits estimate on a three year sales projection that E&R drafted in 1986 for use in a sales presentation to Swarovski. *See* App. 2295a. As these projections were created prior to the sale or manufacture of any Crystal Signatures figurine, the projections were not based on actual sales. In addition, E&R relied on *no* industry information or supporting data in compiling these projections. As such, these projections pale even in comparison to those of the unsuccessful plaintiff in *Advent*, which managed to dress up its claim with sales

projections propounded by two separate and unaffiliated entities. 925 F.2d at 681.

Moreover, Cook took these three year projections and added to them a growth rate for a twelve year period of time, *see* App. 4527a, without any information regarding the crystal or collectibles market, sales of similar items, or the retail industry in general. In *Tunis Bros.*, this Court also faced an instance of rising, speculative sales projections. In that case, the plaintiff's expert projected a 40% increase in the rate of sales of tractors by plaintiffs' franchise in the initial year of the alleged contract, and projected annual increases of more than 10% each year for the following nine years. 952 F.2d at 734. Plaintiff's expert was, however, unable to substantiate these projections with any discernible data other than consultation with the plaintiff itself, which the Court held to be insufficient. *Id.* at 738.

In this case, Cook projected more than a 100% increase in sales in the first year, and annual increases thereafter of more than 20% for the next 4 years, yet Cook had no more basis for substantiating such a growth rate than the expert in *Tunis Bros. See* App. 4527a. For all of these reasons, E&R's damage testimony is irredeemably speculative and wholly insufficient under the law of this Circuit to support the award of lost profits.

D. THE PANEL'S ALLOCATION OF THE ENTIRE $16.5 MILLION PUNITIVE DAMAGE AWARD TO THE SINGLE TORT CLAIM UPHELD IS INCONSISTENT WITH THE LAW OF OTHER CIRCUITS.

The jury's lump-sum award of $16.5 million in punitive damages was based on its liability findings on E&R's

multiple claims of fraud.[7] *See also* App. 1436a (Opinion); 1473-75a. Yet, despite affirming the reversal of judgment on all but one of Plaintiff's claims of fraud, the Panel nonetheless affirmed the $16.5 million in punitive damages in its entirety. The Panel's allocation of the entire lump-sum punitive damage award to only one of the multiple claims on which that award was based is in conflict with the law of other circuits. *See Murphy Door Bed Co. v. Interior Sleep Sys., Inc.* 874 F.2d 95, 104 (2d Cir. 1989); *Litman v. Massachusetts Mut. Life Ins. Co.*, 739 F.2d 1549, 1562 (11th Cir. 1984), *cert. denied*, 484 U.S. 1006 (1988). *See also Midnight Sessions, Ltd. v. City of Philadelphia*, 945 F.2d 667, 687 n.19 (3d Cir. 1991), *cert. denied*, 112 S. Ct. 1668 (1992).[8]

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[7] At trial, E&R argued that it had no less than five separate and distinct claims of fraud against the Swarovski Defendants. *See* App. 3253a-56a; 3337a-41a. The district court grouped these five claims into two separate claims, characterizing the first as fraud against E&R Company (Plaintiff's predecessor in interest) and the second as fraud against E&R Ltd. (the entity created in the leveraged buyout). *Id.* at 1411a-15a (Opinion). The district court granted the Defendants judgment notwithstanding the verdict on the second claim of fraud. *See id.* at 1115a (Opinion).

[8] In *Litman*, the plaintiff obtained an award of punitive damages based on two claims of slander. On appeal, the Eleventh Circuit reversed the judgment on one of the two claims. Based on that reversal, the Eleventh Circuit remanded the punitive damage issue to the trial court for a new trial, stating that "[t]his result is unavoidable in light of the fact that the jury's $250,000 punitive damage award was made in response to a single question on the special verdict form." *Id.* Indeed, because punitive damages are awarded based upon a theory that outrageous conduct should be punished, the court held that the punitive damage award could not be sustained "based partly on the perceived outrageousness of that [nonslanderous]

E. DISPOSITION OF THIS APPEAL BY JUDGMENT ORDER IS A MISAPPLICATION OF THE THIRD CIRCUIT'S INTERNAL OPERATING PROCEDURES, UNFAIRLY PREJUDICES SWAROVSKI'S RIGHT TO SEEK FURTHER REVIEW OF THIS COURT'S DECISION AND DEFAULTS ON THE COURT'S CONSTITUTIONAL OBLIGATION TO REVIEW THE PUNITIVE DAMAGE AWARD.

This Court's Internal Operating Procedures provide that a Judgment Order is only appropriate where the Panel has unanimously determined to affirm the decision, and also determined that a written opinion will have no precedential or institutional value. *See* IOP 6.21; 6.22. The reasons for thus limiting the circumstances in which a Court of Appeals will dispense with a written decision were explained in *National Labor Relations Board v. Amalgamated Clothing Workers of America*, 430 F.2d 966, 972 (5th Cir. 1970):

> Opinions are to serve a number of purposes, at least two of which are highly significant. One is that an articulated discussion of the factors, legal, factual or both, which lead the Court to one rather than to another result, gives strength to the system and reduces, if not eliminates, the easy temptation or tendency to ill-considered or even arbitrary action by those having the awesome power of almost final review. . . .

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statement." *Id. See also Murphy Door*, 874 at 104 (vacating and remanding the punitive damage award because one of the two claims supporting the award was reversed); *Barnes Group, Inc. v. C&C Prods., Inc.*, 716 F.2d 1023, 1034 (4th Cir. 1983) (same).

> The Court recognizes that it must – the word is must – never apply the rule to avoid making a difficult or troublesome decision or to conceal divisive or disturbing issues. This means that while Rule 21[9] should make a real contribution towards the goal of avoiding delays which can often amount to a denial of justice, it must be sparingly used.[10]

The disposition of this case by Judgment Order violates both the letter and the spirit of *Amalgamated* and IOP 6.21 and 6.22. Certainly, in other commercial cases of lesser complexity than this one, the Court has provided the parties with full written opinions even when the judgment of the district court was affirmed.[11] It cannot be said in good conscience that a written opinion in this case would have no precedential value. This Court has taken great pains in *Tunis Bros.* and *Advent* to establish clear limitations on the type and quality of expert testimony

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[9] Fifth Circuit Rule 21, now Fifth Circuit IOP 47.6, is almost identical to Third Circuit IOP 6.21 and 6.22. *See Amalgamated*, 430 F.2d at 968 & n.2.

[10] This admonition necessarily suggests that it will be confined to cases involving well-established legal propositions and/or minor legal consequences to the litigants. Such a disposition would seem particularly inappropriate when applied to a case such as this one, which involves highly complex issues of commercial law, more than 10 assignments of error and a judgment for more than $42 million. Disposition of such an appeal without any explanation to the losing party weakens rather than strengthens belief in the integrity of the appellate process.

[11] *See, e.g., Altronics of Bethlehem, Inc. v. Repco. Inc.*, 957 F.2d 1102 (3d Cir. 1992); *Mellon Bank Corp. v. First Union Real Estate*, 951 F.2d 1399 (3d Cir. 1991); *Sowell v. Butcher & Singer, Inc.*, 926 F.2d 289 (3d Cir. 1991).

necessary to sustain awards of lost profits. This appeal vigorously challenged the sufficiency of E&R's expert testimony under those decisions. An articulation of the reasons why the principles of *Tunis Bros.* and *Advent* were or were not transgressed would have great precedential value to the bench and bar. Similarly, Swarovski presented the Court with a pure legal challenge to the apportionment of the punitive damage award, supported by well-reasoned decisions of other circuits. Whether the Panel distinguished those decisions or disagreed with them substantively, the reasons for that decision clearly have precedential value since there is no prior precedent in this Circuit addressing these authorities. *Cf. Amalgamated* at 972 (admonishing against the use of an affirmance without decision to "conceal divisive or disturbing issues"). Furthermore, the Judgment Order, by obscuring conflicts with decisions both in other circuits and within the Third Circuit itself, prejudices Swarovski's right to obtain in banc review by this Court and a review by the United States Supreme Court.

Moreover, disposition by Judgment Order constitutes an abdication of this Court's constitutional obligation to review the $16.5 million punitive damage award. As the United States Supreme Court has made clear, this Court is constitutionally obligated to make an independent review of the punitive damage award, both as to whether the evidence supports such an award in any amount and whether the amount awarded is greater than that reasonably necessary to punish and deter. *Pacific Mut. Life Ins. Co. v. Haslip*, 111 S. Ct. 1032, 1044, 1045 (1991). Indeed, in *Haslip*, such a review by the Alabama Supreme Court was

an important component of the constitutionality of that punitive damage scheme. *Id.* at 1045.

This Court's failure to undertake and articulate such a review of the punitive damage award is not only a failure of its obligations under *Haslip*, it also hides the legal deficiencies of the $16.5 million award of punitive damages in this case. These deficiencies include the absence of evidence of sufficiently outrageous conduct to justify such a massive award,[12] and the absence of any review of the sufficiency of the evidence supporting the amount of the actual damage award.[13] Indeed, in the face of a $200,000,000 stipulated net worth for Defendants, the trial court upheld a punitive damage award amounting to 8.25% of that figure, a number far in excess of the usual court approved percentage. *See Cash v. Beltmann N. Am. Co.*, 900 F.2d 109, 111 n.3 (7th Cir. 1990) ("[A] typical ratio for a punitive damage award to a defendant's net worth [is] around 1%"). In so affirming this award, the district

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[12] On appeal, Swarovski challenged the sufficiency of the evidence of "outrageous conduct" to support *any* punitive damage award. This Court has held that such conduct must be shown by clear and convincing evidence. *Acosta v. Honda Motor Co.*, 717 F.2d 828, 839 (3d Cir. 1983). Indeed, in *Dunn* this court devoted three pages of its decision to a challenge to the sufficiency of the evidence to sustain a $2 million punitive damage award. Here a $16.5 million award has received no discussion at all.

[13] Obviously, if the actual damage award is itself inflated, the failure to review the evidence supporting that award potentially punishes Swarovski twice by allowing a punitive damage award to stand which would be inherently unreasonable if the actual award were properly limited. E&R's out-of-pocket damages were only $850,000.

court relied on an unsupported "hunch" that the Swarovski's "extreme wealth was far in excess of the amount stipulated," *see* App. 1436a (Opinion at 43), and on the perceived "arrogance" of Swarovski's witnesses, *id.*, a rationale that punishes Swarovski for exercising its constitutional right of access to the courts and has nothing to do with the severity of the alleged wrongdoing itself.

CONCLUSION

For the foregoing substantial reasons, the Swarovski Defendants are entitled to reversal of the judgment under the law of this Circuit. Further, at a minimum under this Court's own procedures and the Supreme Court's ruling in *Haslip*, they are entitled to the articulation of why a $42 million judgment, including $16.5 million in punitive damages, can stand; a process which, we respectfully submit, will demonstrate that the judgment is in error and should be reversed.

Respectfully submitted,

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COUNSEL FOR APPELLANTS AND CROSS-APPELLEES

STATEMENT OF COUNSEL

I express a belief, based on a reasoned and studied professional judgment, that the Panel decision is contrary to the decisions of the United States Court of Appeals for the Third Circuit and other circuits, and of the Supreme Court of the United States, and that consideration by the full Court is necessary to secure and maintain uniformity of decisions in this and other Circuit Courts and the Supreme Court, to-wit, the Panel's decision is contrary to the decision of this Court in *Tunis Bros. Co., Inc. v. Ford Motor Company*, 952 F.2d 715 (3d Cir. 1991) and *Advent Systems, Ltd. v. Unisys Corp.*, 925 F.2d 670 (3d Cir. 1991), the decisions of other Circuits in *Murphy Door Bed Co. v. Interior Sleep Sys., Inc.*, 874 F.2d 95, 104 (2d Cir. 1989) and *Litman v. Massachusetts Mut. Life Ins. Co.*, 739 F.2d 1549, 1562 (11th Cir. 1984), *cert. denied*, 484 U.S. 1006 (1988), and the decision of the United States Supreme Court in *Pacific Mut. Life Ins. Co. v. Haslip*, 111 S. Ct. 1032 (1991).

/s/ William Michael Byrd, Jr.

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing has been served on all counsel of record via United States mail on this the 20th day of April, 1993.

/s/ William Michael Byrd, Jr.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 92-1723, 92-1744

EBELING & REUSS, LTD.
t/a EBELING & REUSS COMPANY,

Appellant in 92-1723

v.

SWAROVSKI INTERNATIONAL TRADING CORPORATION A.G.; D. SWAROVSKI & CO.; SWAROVSKI AMERICA LIMITED; SWAROVSKI AKTIENGESELLSCHAFT

Appellants in 92-1746

Appeal from the United States District Court
for the Eastern District of Pennsylvania
D.C. Civil Docket No. 88-04878
(District Judge: Honorable Norma L. Shapiro)

Argued: March 16, 1993

Before: STAPLETON, ROTH and LEWIS, *Circuit Judges*

JUDGMENT ORDER

After consideration of all contentions raised by appellants,

IT IS ADJUDGED AND ORDERED that the judgment of the district court be and is hereby affirmed.

Each appellant shall bear the costs of its own appeal.

BY THE COURT.

/s/ Illegible
Circuit Judge

Attest:

/s/ P. Douglas Sisk
P. Douglas Sisk, Clerk

DATED: APR 7 1993